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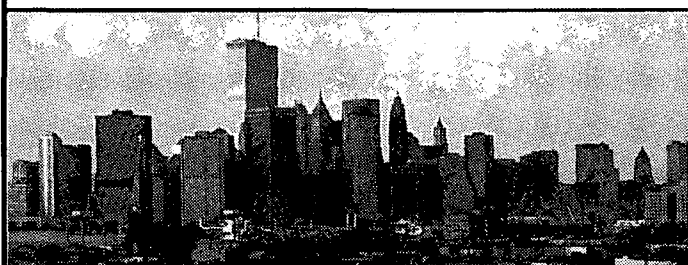
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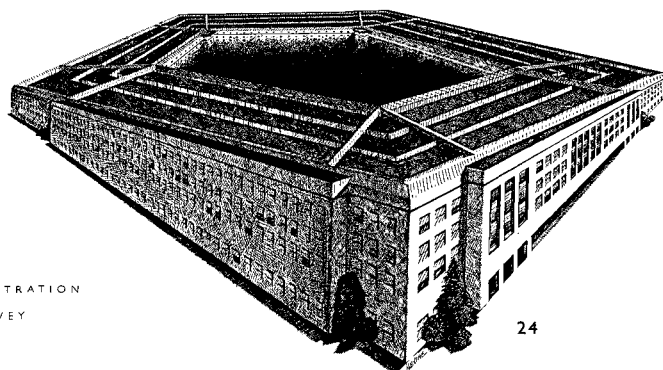
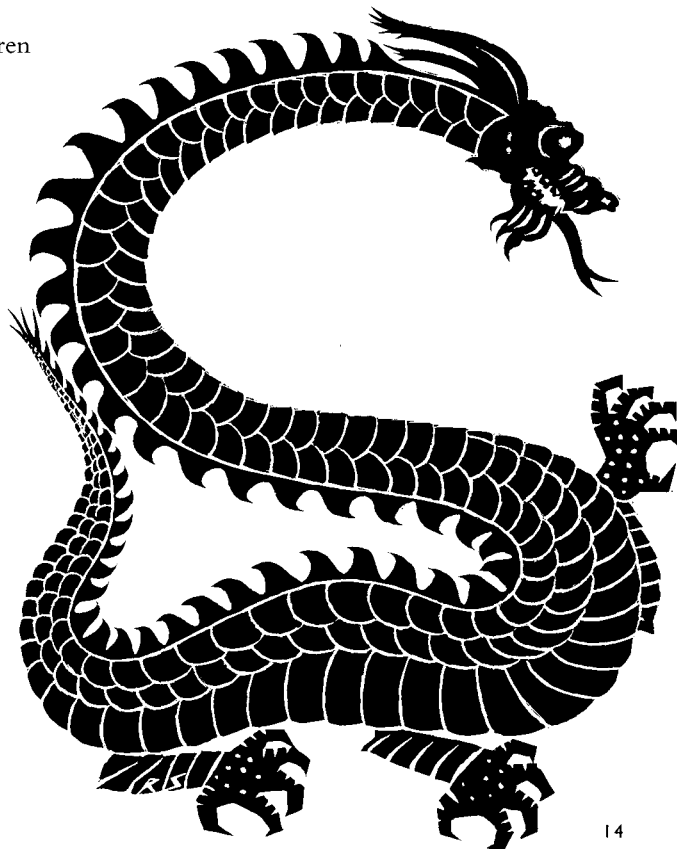
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A Silver Bullet for U.S. Productivity?

■ James Brian Quinn and Martin N. Baily ("Information Technology," summer issue) describe many ways in which information technology has improved service sector performance. They also raise the possibility that the payoffs from massive investments in computer technology would be evident in broad measures of the service sector, if only we had better tools for tracing the economy. If true, this last point would be reassuring, holding out the hope that the economy might be improving faster than official statistics indicate.

But information technology may have had a limited impact on broad measures of economic activity. Computers make up a small fraction (about 2 percent in 1992) of the business plant and equipment used to produce goods and services in the United States. Even if computers were phenomenally productive, their contribution to total economic growth would remain small.

One reason computers are such a tiny share of total plant and equipment is that they become obsolete so rapidly. Much new spending on computers goes to replacing and updating older equipment. The Commerce Department estimates that during the 1980s more than half of the new investment in computers and office equipment was required just to keep up with depreciation, even after taking account of the improvements in the capabilities of computers during the decade.

And although, as Quinn and Baily note, much of the output of information technology is intangible and hard to measure, the difficulty this poses for measuring total economic output can easily be overstated. Many of these hard-to-measure services are purchased by other companies as inputs and are not directly counted as part of gross domestic product (GDP),

which, to avoid double counting, includes only the value of goods and services at the final stage of production.

For example, much of the output of the financial services industry, one of the heaviest users of information technology and hardest to measure, is purchased as inputs by other companies, many of which produce tangible and measurable products. In 1992 financial services, including insurance, accounted for just about 4.5 percent of GDP, after eliminating double counting. Even if information technology has generated a difficult-to-measure explosion in the quality and variety of financial services, this under-measurement probably does not lead to much of an understatement of total economic growth.

Information technology has surely improved performance in some parts of the service sector. Although it would be terrific if these benefits were substantial enough to have a large impact on overall economic growth, information technology may not be a silver bullet for the nation's productivity woes.

Daniel E. Sichel, Brookings

Another Way to Measure IT's Productivity Contribution

■ Although James Brian Quinn and Martin N. Baily ("Information Technology," summer issue) are correct that "aggregate data cannot reliably measure . . . the incremental contribution of IT to productivity," it is nevertheless possible to quantify this contribution and estimate the rate of return on IT investments by performing a statistical analysis of the relationship between IT inputs (quantities of computer equipment and IT employees) and company output (revenues)—holding other inputs constant—across firms within industries. My own such study for the National Bureau of

Economic Research (November 1993) produced findings consistent with the National Research Council study's conclusion that "IT has substantially improved service sector performance." Companies have earned substantial "excess returns" from their investments in both computer capital and computer labor. These inputs jointly account for about 21 percent of output, but only about 10 percent of both capital and labor cost. I also found that the most productive and efficient firms in an industry tend to be the most IT-intensive.

*Frank R. Lichtenberg,
Columbia Business School*

News That Few Want to Hear

■ In "Urban Realities" (summer issue) Tony Downs tells the white urban majority what many do not want to hear: by legal and illegal means—such as exclusionary land use controls and racial discrimination in suburban housing—they have systematically deprived nonwhite minorities of access to jobs, housing, schools, and safe neighborhoods.

As Downs has often explained, only collective action at the state level can make much progress in solving the problem. In most metropolitan areas, a single suburb that opened itself to low- and moderate-income minorities would risk being overwhelmed. But if all the suburbs in a metropolitan area opened up, the effects on most would be modest. An important by-product that has been ignored by scholars would be increased willingness of middle-class whites to live in central cities.

Edwin S. Mills, Northwestern University

The Review welcomes comments from readers. Letters will be edited to conform to style and space.

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Clinton's Foreign Policy Woes: A Way Out

BY LAWRENCE J. KORB

Since coming into office, President Clinton has been under near-constant attack for his handling of the crises in Bosnia, North Korea, Somalia, and Haiti. Ironically, the problem is not his substantive policy decisions—which, indeed, many of his critics support. The problem is that the president has made clear neither the role he wishes this nation to play in the world nor the historical lessons he uses in making his judgments about individual crises.

Four options are available to the United States as it struggles to define its role in the post-Cold War world. First, it can embrace a come-home-America policy focusing on domestic problems. Second, it can aspire to become a 1990s version of the world policeman. As the only remaining superpower, the United States could enforce a Pax Americana, either alone or working with other nations. Third, it can rely primarily on the United Nations to handle world problems. Fourth, it can adopt a policy of pragmatic intervention or selective engagement.

The fourth option posits that the other options have something to offer, but are incomplete. Although the United States should be less involved in the world, it cannot “come home” because without U.S. leadership, the world's problems could get out of control. On the other hand, the United States does not need, nor does it have the resources to handle, all the world's problems. The UN certainly can be used more now that the Cold War is over. But although it can handle peace-keeping operations, its multinational forces are not coordinated enough to handle complex military options.

Clinton has chosen and acted on the fourth option. But in his public discussions he often uses the rhetoric of the first and

third options, confusing both supporters and critics.

A policy of pragmatic intervention is fine in theory, but is difficult to implement without some historical reference points to justify intervention in one case and not in another. Although the president has available to him various historical analogies or tests that he could usefully apply, again his use of them is indiscriminate and confusing.

The first historical analogy is Auschwitz, whose lesson is that evil begets evil and that a nation like the United States, which espouses certain moral principles, cannot, as it did in the 1930s, stand by while “acts of genocide” are committed in places like Bosnia, Haiti, or Rwanda.

The second analogy guiding armed intervention is Sarajevo 1914 (+80), or the Domino Theory. Using this analogy, one could argue that the chief threat today is chaos in the international system, and that the United States must be prepared to use armed force to prevent dangerous or violent situations from spreading and acquiring a momentum of their own. Bosnia thus warrants U.S. concern because if Serb aggressors are rewarded, they may try to incorporate Kosovo and Macedonia into Greater Serbia, perhaps drawing outside powers into the Balkans and leading to a reprise of World War I. Likewise, the United States must be willing to use force to keep nuclear weapons out of the hands of North Korea because a burgeoning nuclear arsenal in Pyongyang could not only give rogue states like Iran, Iraq, and Libya access to such weapons, but also set off a nuclear arms race in Northeast Asia.

Yet another analogy is Vietnam, which raises the question, particularly among U.S. military leaders, whether political leaders can face up to the popular reac-



tion to the military and civilian casualties that will inevitably follow armed intervention. Many military people feel the Vietnam war was won in the field, but lost at home because of the way the media portrayed the horrors of the conflict. The reaction in the United States and the Clinton administration to the death of 18 Rangers in Somalia in October 1993 is evidence that the Vietnam syndrome still survives.

Finally, the Lebanon experience warns the United States about becoming involved in what are essentially civil wars. Both in Lebanon in 1983 and in Somalia in 1993 the United States intervened militarily for humanitarian purposes, but eventually had to take sides to restore enough order to allow the humanitarian effort to succeed. Choosing sides in a civil war can be a recipe for disaster because it antagonizes enough people to make U.S. forces part of the problem rather than part of the solution.

Careful use of these historical analogies could help the president explain and win public approval for his actions. But often he uses the rhetoric of all four analogies simultaneously.

The president must make it clear to the American people that he has chosen a policy of selective engagement that can be costly both in blood and treasure. Then he must rally support for his subsequent actions by invoking the appropriate analogy. Are his actions in Bosnia guided more by Auschwitz and Sarajevo or by Vietnam and Lebanon? Is Haiti a humanitarian or a strategic imperative? Is Rwanda a civil war or genocide? Only the president can say. And he must. ■

Lawrence J. Korb is director of the Brookings Center for Public Policy Education. He is the coauthor of American National Security and Process Policy (Johns Hopkins, 1993).



Somebody's Children

DIANE
RAVITCH

Expanding Educational Opportunities for *All* America's Children



LAST FEBRUARY, IN A SPEECH

on the "State of American Education," Secretary of Education Richard Riley gave America's schools a mixed report card. Some schools, he said, are "excellent, some are improving, some have the remarkable capacity to change for the better." Some, though, "should never be called schools at all."

That last phrase is chilling: schools that "should never be called schools at all." Who attends these schools? African-American and Hispanic children, probably; children from very poor families, probably, many headed by a single parent struggling to make ends meet.

Somebody's children are compelled—some would say, condemned—to attend schools that most teachers shun, if they can, in neighborhoods that people of means avoid, if possible. *Somebody's children* go to those schools. Not mine. Not yours. Not Secretary Riley's. Not President Clinton's nor Vice President Gore's. Not the children of urban mayors or school superintendents or teachers.

Diane Ravitch, a nonresident senior fellow in the Brookings Governmental Studies program, is a senior research fellow at New York University. She is the author, most recently, of National Standards in American Education: A Citizen's Guide (Brookings, 1994). This article is adapted from "Somebody's Children," in Social Policies for Children, edited by Irwin Garfinkel, Jennifer Hochschild, and Sara McLanahan (Brookings, 1995).

Arguments for Means-tested Choice

The strong objections many people have to school choice do not apply to a means-tested choice program. Following are the primary objections raised by choice opponents—and Diane Ravitch's response to them.

1. A CHOICE PROGRAM WOULD DESTROY THE PUBLIC SCHOOL SYSTEM. Opponents of choice fear that if choice were available to all children, huge numbers would leave public education altogether. Such fears are groundless. A Carnegie Foundation for the Advancement of Teaching poll found that only 19 percent of all public school parents would like to send their children to a private school. In a means-tested system, many of these families, of course, would not qualify for scholarships. The public schools would probably enroll 80 percent or more of all students—instead of today's 90 percent. Far from being destroyed, the public school system would be strengthened because it would be able to shut down bad schools.

2. THERE IS NO PRECEDENT FOR ALLOWING STUDENTS TO USE GOVERNMENT FUNDS FOR PRIVATE OR RELIGIOUS INSTITUTIONS. Not true. For many years government-provided Pell grants have enabled college students to attend the school of their choice. The resulting system of higher education is believed by most people to be the best and most pluralistic in the world. The government does not care whether the school attended by a Pell grant student is public, private, or religious as long as it is accredited and approved by its state. Eighty percent of Pell students enroll in public institutions, no doubt because they cost less than private ones. The same dynamic would hold in K-12 education. In addition, religious schools already receive public funds to educate handicapped children and to run Headstart centers.

3. IT WOULD BE UNCONSTITUTIONAL FOR THE GOVERNMENT TO FINANCE RELIGIOUS SCHOOLS. Again, not true. It would be unconstitutional only if a public authority provided funds *directly* to religious

During the course of his speech, Riley invoked John Dewey: "What the best and wisest parent wants for his [and, may I say her] child, that must be [what] the community wants for all of its children. Any other ideal for our schools . . . destroys our democracy."

What would the best and wisest parents do if their children were zoned into schools that are unsafe and educationally bankrupt? They would—if they could—move to a different neighborhood or put their children into private schools. That is what the president did.

But *somebody's children* are required to go to those schools. Parents who don't have the money to move to a better neighborhood or to put their child into a private school have been told that they must stay there no matter how bad the school is. If they are parents with motivation and energy, they are told by school officials and policymakers that they must stay right where they are because they are the kind of parents who might someday help to improve that dreadful school. The people who tell them this would not keep their own child in that school for even a day.

For policymakers and academics, working toward reform "someday" may be appropriate. But for parents it is an outrageous proposition. Parents have children who live today, here and now. They cannot wait around to see whether the school will get better in five or ten years.

As Dewey suggested, we must project our passion for our own children's welfare onto those desperate parents. They love their children as much as we love ours. They worry about their children's future—and they know how much the odds are stacked against them. They should not be expected to wait patiently for the eventual transformation of the failing schools their children are required to attend each day. We would not thus sacrifice our own children. Why must they?

We Can't Wait for "Someday"

What can we do—and do *quickly*—for the children now attending schools that should not be called schools? The best solution I see is for states, cities, or the federal government to provide means-tested scholarships to needy families, who may use them to send their children to the school of their choice, be it public, independent, or religious.

The size of the scholarship should vary in relation to family income. The needier the child, the larger the grant. For the neediest, the grant should be at least equal to the state average per pupil expenditure, possibly larger. Children with disabilities should receive the full amount of financial aid to which they would be entitled under state and federal law. Since funds will necessarily be limited, highest priority for such scholarships should go to children who are now enrolled in schools identified by public authorities as the worst in the district. The number and size of such scholarships can be strictly controlled by public authorities to gauge the cost and consequences—though the number and size must not be so small as to render the program meaningless.

This proposal is not new. Others have made it before. It is, however, new for me.

For years I could not make up my mind about the issue of school choice. Unlike some supporters of choice, I harbor no animus toward the public schools. I attended public schools in Houston, Texas, for 13 years. I consider myself a friend and supporter of public education. But several things have overcome my hesitation about choice. First and foremost is that many years—and wave after wave of reforms—have passed, leaving the most desperate inner-city schools fundamentally unchanged. Trying harder has helped some schools, but the worst are untouched.

Certain personal experiences were also decisive. While in London in the fall of 1992 I visited one of Britain's "grant-maintained" schools—schools where parents have voted to leave the jurisdiction

of the local board of education and receive public funding directly from the national government. The school I visited was a Roman Catholic girls' school, most of whose students were members of racial minorities. The nun who showed me around was in street dress, as were the teachers. The money that had once gone to the local school board (about 15 percent of the school's budget) now went directly to the school. The added funds helped build a new science laboratory, make long-deferred repairs, and hire more teachers. For the first time in its history, the school was allowed to select its own food supplier. No longer the last link in a bureaucratic chain, the staff in the school made their own decisions. In classroom after classroom I saw teenage girls preparing for the national examinations in an atmosphere that was orderly, cheerful, and well-maintained. I vividly recall the guide's comment: "You can always tell a grant-maintained school by the smell of fresh paint."

Separation of Church and State?

That visit raised some questions. In the United States opposition to funding nonpublic schools, especially religious schools, is powerful. Admitting any demonstration of religious faith into the public school is anathema. We have been told for years that using any public funds in a religious school violates the constitutional principle of separation of church and state. Why?

No other developed democracy that shares our ideals has such a "wall of separation." Every other Western nation provides state aid to religious and other private schools. Denmark's government, for example, directly funds nonstate schools so that parents can exercise religious and political freedom. Only a tiny minority—about 5.6 percent—choose to attend such schools.

Why do we alone adamantly refuse any public funding for children who attend religious schools? And why only at the primary and secondary level? Why is Mary Jones—a young woman from an impoverished family—ineligible for public funds when she is an 18-year-old senior at St. Mary's Academy, yet eligible for a federal Pell grant when she is an 18-year-old freshman at St. Mary's College? Is it fair to deny free education to needy citizens whose religious convictions make it impossible for them to send their children to secular state schools? Why is public funding available only to schools that exclude religious values? Why is there free speech in public schools for all controversial views except religious ideas?

Although the rise of the American common school during the 19th century is often traced to efforts to create secular schools, in fact the goal of the evangelical Protestant reformers behind the movement was to deny public funds to Catholic schools and to assure that public funds went solely to nondenominational Protestant schools. And they succeeded. Well into the 20th century, students in nonsectarian public schools read the Protestant Bible, sang Protestant hymns, recited Protestant prayers, and learned a Protestant version of European history.

As historian Lloyd Jorgenson notes in *The State and the Nonpublic School, 1825–1925*, common school reformers did not claim that it was unconstitutional to spend public funds in Catholic schools. Instead, they passed state laws to prevent it. They did not invoke the principle of separation of church and state. Rather, they charged that Catholicism was a "menace to republican institutions and must be curbed." In short, America's common school ideology is rooted firmly in anti-Catholic bigotry.

All Our Children

The resulting theory of public education developed over the years is unnecessarily constricted. Public education, in current theory, happens only in schools operated and controlled by the government. Yet what should concern us is the education of

schools. Financial aid that goes to parents to spend at the school of their choice would not violate the principle of separation of church and state. A 1971 court ruling established a three-prong test to determine the constitutionality of legislation affecting church-state issues. The statute must have a secular legislative purpose; its principal effect must neither advance nor inhibit religion; and it must not foster "an excessive governmental entanglement with religion." A law that grants funds to parents, not to religious schools, would meet all three requirements. In 1986 a unanimous Supreme Court upheld the grant of state aid to a blind student attending a Bible college in preparation for being a minister. In 1993 the Court ruled a public school district could provide a sign language interpreter for a deaf student in a Catholic high school. In both cases the ruling turned on the fact that the parents had made the choice.

4. A CHOICE SYSTEM WOULD PUT AN INTOLERABLE BURDEN ON ALREADY STRAINED STATE AND LOCAL BUDGETS. A means-tested choice program would involve measurable, predictable, and limited spending. It would cost the public no more than states now spend for children in public schools.

A full choice program may actually be a money-saver on capital expenditures. U.S. school enrollments are again on the rise. By 2004 they are expected to grow 13 percent in grades K–8, 24 percent in grades 9–12. Public officials must make a choice: either invest billions of dollars to build new schools or use fully all existing facilities. Officials can do the latter through a choice system that is well organized, well supervised, and coordinated with existing public schools.

5. A CHOICE PROGRAM WOULD "CREAM OFF" THE BEST STUDENTS, LEAVING PUBLIC SCHOOLS WITH THE POOREST AND MOST DIFFICULT STUDENTS. In a means-tested choice program, scholarships would be given only to the poorest students in the worst schools. Good schools in big cities will not be hurt by a means-tested choice program; they are likely to get many more applicants. Their students do not want to leave; their parents know they are getting a good education.

6. A CHOICE PROGRAM COULD WORSEN SEGREGATION IN BIG-CITY DISTRICTS. Providing means-tested scholarships to African-American and Hispanic students enrolled in completely segregated inner-city schools may well reduce segregation. It cannot make it worse.

7. A CHOICE PROGRAM COULD USE PUBLIC FUNDS TO SUPPORT SCHOOLS THAT TEACH BIZARRE RELIGIOUS AND RACIAL IDEAS.

This potential problem would be easy to solve. Schools that violate civil rights laws or that teach racial or religious hatred would not be eligible to receive public scholarships. And schools that accept public scholarships would have to prepare their students to pass state subject-matter assessments at rates no worse than comparable public schools.

8. NONPUBLIC SCHOOLS MAY SHUN STUDENTS WITH HANDICAPPING CONDITIONS. Students with special needs should be eligible for a scholarship to go where their needs can best be met. If the scholarship is large enough, new schools will be created to meet the needs of these children. The Supreme Court has already ruled that parents of disabled students have the right to a free publicly financed education in the private sector if the state cannot provide it.

9. HOW CAN PUBLIC AUTHORITIES HOLD NON-PUBLIC SCHOOLS ACCOUNTABLE? Public authorities will find it easier to ensure the accountability of both nonpublic schools and public schools under a means-tested choice program. They now have no leverage over failing public schools. They cannot punish them by taking away money; that only makes matters worse. They have tried—without success—threatening to take the schools over or to send in monitors. If authorities could offer scholarships to students trapped in terrible schools, it would give them leverage over those schools while protecting the students. In a means-tested choice system, if nonpublic schools and public charter schools fail to meet their contractual obligations, officials can revoke their charter or their eligibility to receive public scholarships.

10. IT IS SOCIALLY DIVISIVE TO ALLOW STUDENTS TO ATTEND SCHOOLS WITH DIFFERENT VALUES. Actually, our most divisive school-related conflicts occur because we impose a single set of state-defined values on everyone in public schools. School boards make decisions

the public—all the public. And what should concern us most is the education of children who are at risk, whether they go to a public school or not.

The best way to provide educational opportunity for poor children in urban areas is to make available means-tested scholarships with priority for children who are enrolled in schools with a long-term record of poor performance, to be used in the schools of their choice. If the scholarships are generous enough, many schools will welcome scholarship students, and new schools will open to supply the demand for good education.

Even the best schools cannot do everything to protect at-risk young people from the pressures that threaten them—from poverty, teen pregnancy, drug and alcohol abuse, AIDS, homelessness, violence. Even the best schools cannot by themselves end poverty—although children who do not get a good education are likely to endure a lifetime of poverty. Even the best schools cannot by themselves create jobs or improve housing conditions or stop the violence on the streets. But schools can and must nurture and guide the young people who are growing up in a milieu fraught with peril.

The anonymous comprehensive high school, for example—a hallmark of American education for most of this century—cannot meet the needs of endangered youngsters in the cities. Those children need individual support and nurturance. They need schools that work closely with their families. They need schools where many adults know their names and care about them, know when they are absent, know when they have a problem, think about their future, and talk frequently to their parents or guardian.

Whether public or private, the most successful urban schools share certain characteristics. Paul Hill calls them “high schools with character.” TheodoreSizer calls them “thoughtful places.” In their recent book about Catholic education, Anthony Bryk, Valerie Lee, and Peter Holland describe the caring community created by Catholic schools. All have in common a sense of purpose, a mission, an identity of their own. And all function *in loco parentis*, with the knowledge and assent of parents who welcome a partnership with the school.

There are two ways to create more such schools. One is to provide means-tested scholarships to poor children, allowing them to attend any school that accepts public accountability for educational standards and civil rights laws. The other is to promote the spread of charter schools and special-purpose public schools managed under contract by institutions, parents, and teachers. The charter school movement is spreading rapidly. It has already been adopted in nearly a dozen states, is being considered by nearly a dozen more, and has been endorsed by the National School Boards Association. It is a politically practical strategy that avoids the inevitable constitutional problems that will accompany any choice plan that includes private and religious schools. But the two strategies are not alternatives. Rather, they are complementary ways to create a more diverse, pluralistic system of good schools from which parents and students may choose. One creates demand for special-purpose schools by supplying scholarships, the other creates a new supply by encouraging the spread of special-purpose schools.

Both strategies would expand educational opportunities for poor children. I argue the case for choice involving both state and non-state schools for two reasons. First, opening choice to all schools will rapidly expand the supply of places available. Second, including private and religious schools, so long as they are willing to comply with state standards, is a matter of justice. It is not *just* to compel poor children to attend bad schools. It is not *just* to prohibit poor families from sending their children to the school of their choice, even if that school has a religious affiliation. It is not *just* to deny free schooling

to poor families with strong religious convictions, any more than it would be just to prohibit the use of federal scholarships in nonpublic universities like Notre Dame, Marymount, or Yeshiva. It is not *just* that there is no realistic way to close schools that students and their parents would abandon if they could.

What a Means-Tested Choice Program Could Do

What difference could a means-tested choice program make in the life of children now compelled to attend schools that should never be called schools? First, and most important, it would free those children to move to better schools—public, private, or religious. As the charter school movement spreads across the country, opportunities for students to move to small, purposeful schools are increasing. A model school created by Wayne State University in Detroit was heavily oversubscribed. Rice University in Houston was inundated with applications for a new school near its campus. Catholic schools have a strong track record, especially with disadvantaged urban students, who have a lower dropout rate and higher test scores than their peers in public schools. One reason for the difference is that students in Catholic schools are much likelier to be placed in college preparatory programs, regardless of race or social class. In 1990, 66 percent of high school sophomores in Catholic schools—and only 39 percent in public schools—were on a college-bound track.

Second, a means-tested choice program could strengthen the role of families in the lives of these children by giving parents a greater say in their children's education. Parent participation is certainly much greater in Catholic schools than in public schools, and it is probably greater in "focus" public schools than in ordinary public schools. Parents of children in Catholic schools are twice as likely as public school parents to belong to and participate in the PTA. Parents of poor black students in Catholic schools participate in the PTA at much higher levels than their counterparts in public schools. The act of choosing a school seems to make parents feel more responsible and become more involved.

Finally, means-tested scholarships will enable students to attend schools where teachers and parents share values and agree on a code of conduct. Participating in a close, consensual community will help nurture youngsters and shelter them from the dangers of the street. Most public schools, now operating on the basis of hierarchical, bureaucratic rules and regulations, fail to engage students as members of a community. Means-tested scholarships will enable eligible students to attend a school where there is focus, mission, and identity. Only in such a setting can students who are now alienated begin to see themselves as responsible participants, surrounded by adults and other students who are affected by their decisions and actions. Under the current system, there is no incentive to establish new focus schools. In a choice program, the incentive is to create many such schools.

Everybody's Children

Perhaps more than the people of any other nation, Americans value the freedom to choose, to make their own decisions, to manage their own lives. Children growing up in neighborhoods their parents cannot leave, attending schools no one would willingly attend, have no choice at all—about a matter of enormous consequence in their lives.

The goal of my proposal is to create a diverse, pluralistic system of schools with many different kinds of sponsors, all dedicated to educating the public and all monitored by state agencies responsible for assuring both equity and excellence. *Nobody's children* should be compelled to attend a bad public school. A good school system must offer equal education opportunity to *everybody's children*. ■

that are deeply offensive to some families. Those of us who are liberal and secular feel comforted when our side wins and frightened when the other side wins. Yet why must people who are not liberal and secular submit their children to values they find oppressive? Under a means-tested choice program, schools should differ from each other in a variety of ways, so long as they respect the Constitution and the laws of the state and satisfy the state's educational standards. Permitting diversity of values may well prove less divisive in the end.

11. HOW WILL NEWCOMERS TO THE UNITED STATES BE ASSIMILATED TO THE MAINSTREAM IF THEY GO TO ETHNIC OR RELIGIOUS SCHOOLS?

Most new immigrants will continue to choose traditional public schools because they are free, convenient, and satisfactory to most parents. Those who do not choose public schools do not threaten the stability of the nation. There is no reason to believe that children who attend nonpublic schools are any less civic-minded as adults than those who attend public schools. In fact, the public schools may not be the primary means of civic assimilation in our society. American society itself—its laws, its cultural pluralism, its openness, its tolerance for diversity, its encouragement of freedom of expression—may be the most effective instrument of social assimilation. Our commitment to pluralism and diversity should be strong enough to tolerate the few devout separatists who do not wish to assimilate.



Eric A. Hanushek

MAKING AMERICA'S SCHOOLS WORK

This Time Money Is Not the Answer

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No one is happy with America's schools. Students, parents, politicians all call for schools to do a better job. The news media regularly report the failures of U.S. education, whether in the poor showing of American students in international test score competition or in the deficiencies of graduates entering the workplace.

Often the blame is placed on tightfisted government officials and taxpayers. Teachers' salaries, it is said, are too low. Class sizes are too big. The school year is too short. Educational reformers emphasize the need for renewed commitment to schooling—a commitment that is often translated into an appeal for expanded resources for schools.

But in fact, the nation has been spending more and more to achieve results that are no better and perhaps worse. Between 1960 and 1990, while student performance on such tests as the SAT and the National Assessment of Educational Progress faltered, real (inflation-adjusted) public spending on elementary and secondary education in the United States rose from just over \$50 billion to almost \$190 billion. Real per-student spending more than tripled—from \$1,454 in 1960 to \$4,622 in 1990.

Surprisingly, the increased costs, combined with public dissatisfaction with school performance, have aroused few protests or demands to stop the growth in spending. One explanation for the public's silence may be that the dramatic 1970–90 drop in the school-age population masked overall spending increases by offsetting much of the rise in per pupil instructional costs. But if that is the case, trouble lurks on the horizon. For the population of school-age children is on the rise again, and with it, fiscal pressures.

America's lunar-landing approach to school reform—devote sufficient energy and resources to the problem and the nation will crack it—is not sustainable. Education faces stiff competition for society's limited resources. The nation will not, indeed cannot, continue to spend more and more on education to achieve flat or falling performance.

More Money, Better Schools?

Nor is there any *reason* to continue to pour ever more money into the schools, given their current organization. Over the past quarter century researchers have made the surprising discovery that there is little systematic relationship between school resources and student performance. For every study that finds that increases in basic school resources promote higher achievement, another study shows just the opposite.

Take class size, for example. The intuitively appealing idea that smaller classes will improve student learning is a perennial cornerstone of educational reform. As a result, the pupil-teacher ratio in American schools is always on the decline. The ratio, which stood at 35–1 in 1890, fell to 28–1 in 1940, 20–1 in 1970, and less than 16–1 in 1990.

But econometric and experimental evidence shows vividly that across-the-board reductions in class size

are unlikely to yield discernible gains in overall student achievement. That is not to say that small classes are never useful. Some situations may lend themselves to smaller classes, while others can accommodate larger classes. For example, individual tutorial programs can substantially improve the achievement of poorly performing primary school students, while other students in various situations can be placed in larger classes without jeopardizing their achievement—so holding overall cost constant. Indeed, in Japan teachers and administrators expressly trade large class sizes for more time for teacher preparation. But so far, U.S. schools have made little effort to learn which uses of resources, for smaller classes or other purposes, best promote student achievement.

As the public school system is now organized, some schools appear to use money and resources effectively, but others do not. In fact, resources are spent ineffectively so often that there is simply no reason to expect overall improvement from increased resources. School administrators today are not monitoring the performance of their programs or the effectiveness of resource use. Schools have no way to know what does and does not work. What's more, few incentives push toward improved schooling and higher student performance.

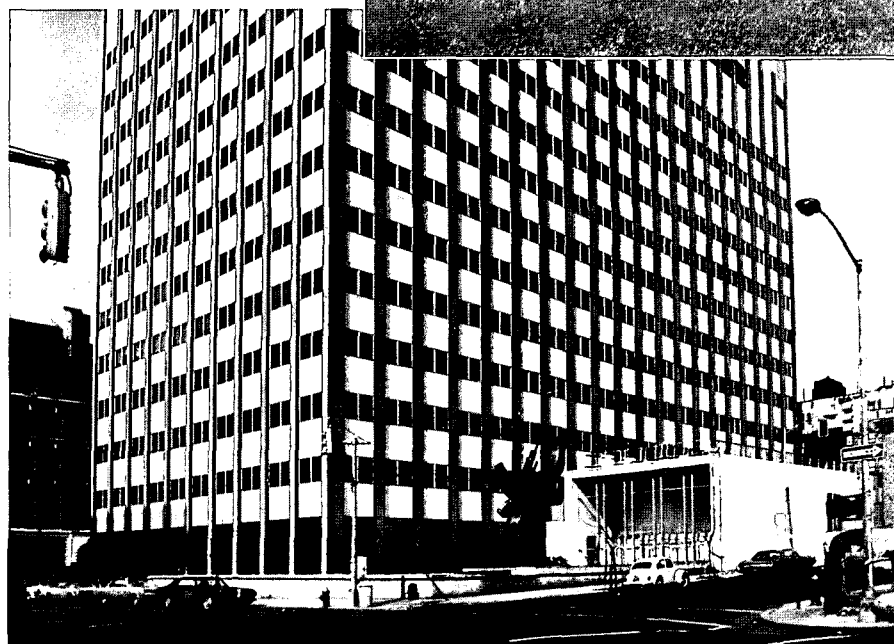
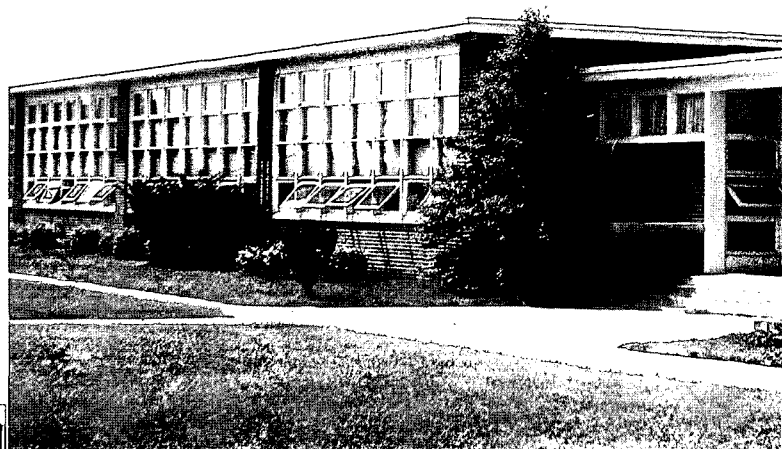


Put the Money Where It Works

The highest priority for America's schools today is to use existing resources more efficiently. When economists try to interject the economic principle of efficiency into the education debate, however, they often meet with stout resistance—largely because of misunderstandings. Efficiency does not mean that educators should undertake a relentless drive to cut costs. Rather, it means that they should measure both the costs and benefits of various approaches to education—and choose the approach that maximizes the excess of benefits over costs. In simplest terms, funds devoted to schools should be put to their best possible use. If two programs are competing for limited funds, put the money into the one that achieves the best results. If a program does not improve student performance, do not fund it.

These notions are so commonsensical that resistance to them would seem out of the question. But as America's schools are now run, virtually no one in them has a serious interest in improving performance or conserving resources. And all are reluctant to face the uncertainty that change would entail.

The best way to improve performance is to establish mechanisms that directly reward improvement. In general, school systems can be run in two ways: through regulation and through performance



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incentives. Regulation is a centralized command and control system. Central management creates a system of rules. Results can be satisfactory if the rules are appropriate and useful, if the schools can be adequately monitored, and if punishments for violating rules are sufficient to ensure that rules are obeyed. Performance incentives, on the other hand, rely more on rewards within a decentralized system of decisionmaking. Central management specifies its goals and rewards those who achieve them. Typically, incentive systems specify what is to be achieved and leave it up to the agent to decide how, while regulatory regimes attempt to specify both what and how.

Today's schools rely far more heavily on regulation than on incentives, even though education is inherently a highly decentralized activity. Almost all productive work is done in classrooms. It is next to impossible to create a single set of regulations capable of identifying, hiring, and mobilizing America's almost 3 million teachers. Still, despite the evident difficulty of applying strong regulatory regimes to education, schools today make little use of performance incentives—with results that are all too evident.

People respond to incentives, be they financial, emotional, or some other form. When rewarded for an action, people do it. Students, teachers, and other school personnel are no different. Moreover, every organization, either implicitly or explicitly, sets up incentives for action. Unfortunately, few incentives within today's schools relate to student performance. If school reform is to work, that must change.

Learning about Incentives

It is not enough simply to exhort schools to “use performance incentives.” Performance incentives come in many forms, and incentives that work in one school system may not work in another. If there is a single, glaring lesson to be learned from past attempts at school reform, it is that no single overarching reform can solve the problems of every school. Policymakers must decentralize school systems to allow local decisionmakers to devise programs appropriate for their situations. They must also help provide the discipline to ensure that those programs are effective.

The school reform landscape is dotted with proposals for new programs of educational incentives. The ideas behind them are conceptually appealing, but so far we have little experience with the programs in practice. Somewhat hesitantly, schools have begun to

experiment with a variety of new programs that differ both in how they define “good” performance and how they reward it. For example, charter schools enable teachers to set up new schools to try out new educational ideas in exchange for performance commitments. School choice and educational vouchers give students and their parents an important voice in determining whether schools are good by allowing them to decide which to attend. Merit pay for teachers and principals, together with attempts to contract educational services to private firms, provide still other performance definitions and incentives.

Applications of these new programs have, nonetheless, been very limited. All will need to be tested far more widely, and much greater effort will have to go into evaluating their performance and disseminating information about their results. The field of medicine has made great strides by wide and systematic experiments to test the efficacy of new treatments and publicize their success or failure. Schools should do likewise.

In some ways the discussion about performance incentives has become confused with notions of decentralized decisionmaking. Considerable legislation and local change has been devoted to promoting decentralized decisions through such means as site-based management or semi-autonomous subdistricts. But decentralization alone is not enough—for it has been tried widely and has frequently failed to lead to general improvement. Decentralization must be combined with well-crafted performance incentives based on clear definitions of good performance. These definitions, in turn, require agreement on the goals and objectives of schools.

Measurement and Evaluation

An essential ingredient of reform will therefore be clear measurement of student performance—a subject that is itself controversial. Naturally, people differ on what they think schools should accomplish, on how those things are best evaluated, and, ultimately, on what part of student performance should be attributed to schools.

The starting point must be a plain delineation of goals and objectives. While defining a good education is politically difficult, performance in core academic areas should be paramount. If schools fail to prepare students properly with basic literacy, numeracy, and analytical skills, they will never be judged successful.

One aspect of performance measurement that is being hotly debated is the appropriateness of currently available standardized tests. Many participants in that debate, however, can agree on three points. First, good measures of student performance are essential to educational improvement. Second, while the appropriate testing instrument depends considerably on the purpose of measurement, existing tests, though far from perfect, do provide useful information in assessing schools' performance. Third, although test measurements can and should be improved, evaluation of schools should not await development of the perfect instrument.

One confusion about performance measurement involves judging the contribution of schools. When

student test scores are made public, many people immediately judge the performance of schools solely on the basis of these scores, implicitly ignoring the fact that student performance is the result of much more than just the schools. Inevitably it involves a mixture of schooling, education in the home, innate abilities, and the like. Thus, for example, a teacher or school that must deal with students unprepared for their current grade level should not be penalized for poor student preparation. Instead, attention should be focused on what the teacher or school contributes—on their value-added to learning. This focus is particularly appropriate when student performance is incorporated in incentive systems. Concentrating on value-added is also essential to program evaluations that attempt to uncover effective approaches to schooling. Indeed, when value-added is appropriately measured, we may well find that some schools with high average scores are really contributing little to students' performance and vice versa.

Altered Roles

Moving toward a school system that uses resources effectively, emphasizes incentives, and recognizes the importance of evaluation will require all participants to take on new roles and responsibilities, which will, of course, vary across states and districts.

Teachers, perhaps the most important element of our schooling system, must take an active part in improving schools. Yet teaching under a new system based on performance incentives and decentralized decisionmaking promises different challenges—and requires new experience, training, and expectations—than teaching today. One way to introduce changes into teaching without completely alienating current teachers is two-tier employment contracts. New teachers' contracts would offer fewer tenure guarantees, more risks, and greater flexibility and rewards. Existing teachers could either continue under existing employment rules for tenure, pay, and work conditions or opt for the new-style contract. The expectations that today's teachers had when they entered the profession cannot be arbitrarily revoked if we expect schools to improve.

State governments should put aside many of their old tasks—laying down school curricula and procedures—and instead promote local experimentation with new incentive systems and then help produce and disseminate evaluation results. States should define performance standards and explicit student goals. Finally, states share with the federal government a role in ensuring equality of opportunity. Disadvantaged students may well require additional resources, even when all schools are using resources effectively. Moreover, states must monitor the performance of local districts. When performance is unacceptably low, states must intervene through school choice programs or voucher systems that will enable students in poorly performing districts to move to better schools elsewhere.

The federal government should join states in setting goals and standards, developing performance information, supporting evaluation, and disseminating results. It should also take the lead in supporting supplemental

programs for disadvantaged and minority students. (Programs for the disadvantaged should themselves follow the same guidelines as all other programs but may also involve expansions of earlier childhood education, integrated health and nutrition programs, and other supplemental interventions.)

Local school districts' responsibilities—making curricular choices and managing teacher and administrative personnel—would remain nominally the same but would actually change significantly if states removed many of their restrictions on instruction and organization. Moreover, if major decisions devolved to local schools, new emphasis would be placed on management and leadership.

Businesses too could take on a new role. While businesses frequently lament the quality of workers being turned out by the schools, they have never worked closely with schools in defining the skills and abilities they want. Closer consultation with schools, perhaps coupled with long-term hiring relationships, could aid both schools and businesses. Moreover, businesses could give students valuable incentives to perform well in school by making it clear that hiring decisions are based on school transcripts. And experienced business managers might have much to teach schools about how to manage performance incentives.

Finally, parents, who often have few opportunities to play an active part in schools today, would have a crucial role in many incentive-based systems of school management. Systems of choice require parents to decide which school offers the best opportunities for their children. Systems of decentralized management give parents a chance to become more actively involved in running schools, and indeed may require it.

An Overriding Perspective

Reforming America's schools does not require more money. On the contrary, the cause of reform will best be advanced by holding overall real spending constant. Schools must acquire the discipline imposed by economic efficiency. They must learn to consider trade-offs among programs and operations. They must learn to evaluate performance and eliminate programs that are not working. They must learn to seek out and expand on productive incentive structures and organizational approaches. In short, they must make better use of existing resources.

Inefficiencies in the current structure of schools are widespread, but there is little interest or pressure to eliminate them. Where such interest exists, it is often thwarted by regulations or contract restrictions that do not permit reasonable adjustments in personnel, classroom organization, the use of new technologies or other approaches that might improve performance for existing spending. If America's schools are to improve, they must embrace the basic principles of economics, with its attention to effectiveness of expenditures and to establishing appropriate incentives.

In the long run, the nation may find it appropriate to increase school spending. It is simply hard to tell at this point. But it is clear that expanding resources first and looking for reform second is likely to lead only to a more expensive system, not a better one. ■

A
STRONG
CHINA

IS THE UNITED STATES READY?

East Asians don't know quite what to make of China these days. Their expanding involvement in China's rapidly growing economy is making them rich. But it is also helping to make China strong. Leaders in Beijing are already claiming border areas and offshore islands with a new assertiveness and buying weapons from Russia capable of backing those claims with force. As one Singaporean diplomat told American researcher David Hitchcock last year, "All of Southeast Asia is scared" by the growth of China's power.

Americans too seem to be worrying more about China. Beside longstanding concern about China's arms sales to "backlash" states and its poor human rights record now stand visions of China as an "awakening dragon" preparing to assert its dominance in East Asia. Samuel Huntington writes of a Sino-centric Confucian civilization headed for conflict with the West—a threatening China that must be contained, much as the Soviet Union was during the Cold War.

How seriously should we take the notion of a "threat" from China? Alarmists would seem to be exaggerating. China's military is huge but also vastly underdeveloped doctrinally and technologically. That will change if present trends continue, but recent double-digit economic growth, while striking, is probably unsustainable. At least as plausible as an "awakening dragon" is a China plagued by economic decentralization and political decay and thus unable to exploit its enormous power potential. Finally, since 1978 China's leaders have sought a stable and friendly international environment to encourage economic growth. They have solved their once-rancorous border dispute with Russia and shelved their territorial disputes with India. Far from being a threat, today's China would seem to confirm liberal claims that economic growth and interdependence encourage cooperation and conflict resolution.

Yet China's growth is indeed worth worrying about, not because it will surely continue, nor because a strong China will seek to dominate its neighbors, but because if China continues to grow it will confront the world with a change in power relationships of unprecedented size, ultimately involving the emergence of a power capable of overshadowing Japan, perhaps even the United States. In the past, large power transitions have been marked by instability and conflict. China's ties to the global economy may soften this one. But if not, China's growth is likely to threaten regional stability—a vital U.S. interest—regardless of China's intent.

China's growth is already tweaking insecurities around East Asia. And while East Asians will try to cooperate in balancing and containing China's power, lingering suspicions and an underdeveloped regional security structure obstruct such alliances. Although China is years away from posing a serious direct military threat to the United States (assuming it wants to), the destabilizing effects of its growth could easily find their way to the U.S. doorstep.

Are U.S. policymakers ready to deal with an increasingly strong China? They have no historical precedents on which to draw for guidance, since for much of U.S. history China was in decay or collapse, while during the Cold War China remained in the shadow of Soviet power. Today U.S. policymakers have the same problem China's neighbors do. They are happy to help China get rich, since the process adds to U.S. wealth. They just wish that making China rich did not also make it strong. Alas China may grow strong anyway. It is doing so now, and its emerging strength is already straining U.S. policy responses. It's time to think through the implications of a strong China.

The Dilemma of China's Growth

Even though China's leaders profess to threaten no one, China's military growth ensnares its neighbors in a classic "security dilemma." Unsure of China's intentions, changeable in any case, they look at China's capabilities. And these, now huge but backward, are growing more worrisome.

Availing itself of Russia's willingness to sell weapons at bargain-basement prices, China is modernizing its forces and extending their range. Alongside newer tanks are long-range fighters, a more seaworthy navy, and more sophisticated amphibious assault capabilities. Such purchases reflect mid-1980s doctrinal changes emphasizing greater mobility and firepower for ground forces and projection capabilities for sea and air forces. Against the background of Mao's doctrine of people's war, which relied largely on infantry defense, the new trend in weapons and doctrine inevitably appears threatening.

Ironically, Russians are among those most worried. Russia's vastly underpopulated Far East has always been a logistics nightmare for Russian forces. Against a strong China, Russians worry that their Far Eastern border is almost indefensible. That problem helps explain the conspicuous absence of a nuclear "no-first-use" pledge from Russia's new military doctrine. Like NATO during the Cold War, Russians think they may have to rely on nuclear weapons to compensate for conventional force inferiority.

China's fledgling arms buildup has also begun to stir

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Japanese anxiety about vital sea-lanes in the South China Sea. Reportedly Japanese diplomats have warned Moscow about its arms sales to China. They may also have threatened economic retaliation had China purchased an aircraft carrier from the Ukraine (China has dropped the carrier idea, at least for now, although its reasons remain unclear). The U.S.-Japan security relationship allays concern in Tokyo, but any withering of that relationship while China's force buildup continues could start a Sino-Japanese arms race.

The Burden of History

For some of China's neighbors, the security dilemma posed by China's growth is compounded by ancient territorial disputes. Japan, China, and Taiwan, for example, all claim a small island group (called Diaoyutai in China, Senkaku in Japan) northeast of Taiwan. A potentially much more serious dispute involves Outer Mongolia, independent now but part of China two centuries ago. At times in this century Chinese leaders as diverse as Sun Yat-Sen, Mao Tse-Tung, and Chang Kai-Shek all referred to Outer Mongolia as part of "greater China," and in 1921 China tried to back its claim by force, but was repelled by Soviet troops. Today Beijing recognizes the Republic of Mongolia, but Outer Mongolians, shorn not only of occupying Soviet forces but of a strong Russia to play off against a growing China, still worry.

For the moment, the "front-burner" dispute involves the Spratly islands, on the southern edge of the South China Sea. Its historical claim sharpened by its interest in the offshore area's minerals, China claims all these islands and thus virtually all the South China Sea. But Taiwan, Vietnam, Brunei, Malaysia, and the Philippines claim at least some of the same islands and undersea resources.

Beijing has promised not to use force to settle the dispute and has declared itself willing to co-develop the area's resources with other claimants, but its actions undermine its rhetoric. For 20 years China has slowly extended its occupation of various islands southward. It used force in 1974 and again in 1988 to wrest key islands from Vietnam. And it has continued developing military bases in the area. In February 1992 China's People's Congress claimed the Spratlys more forcefully than ever before, authorizing military action to defend those claims. China also hired a U.S. firm to explore for oil on islands on what Vietnam claims is its continental shelf.

It is correct but not very comforting to other claimants to note that China's military remains under-

developed, even in comparison with many Southeast Asian militaries. China doesn't need aircraft carriers to assert authority in the South China Sea; it has proximity and island bases. It doesn't need sophisticated tanks to worry the Russians; it has relative mass. China's 1979 invasion of northern Vietnam may have been a tactical debacle, but it was strategically successful, when combined with China's support to Cambodia's Khmer Rouge, in squeezing Vietnam between threats in two directions.

Above all, China has time—if it continues to grow. In that case it will slowly outstrip its neighbors in economic as well as military might. The uncertainty helps explain the low-key reaction of China's neighbors to the Spratlys dispute. They are buying arms, at least partly because of concern about China, but too slowly yet to call the purchases an "arms race." Most have also deployed forces and built military bases or even resort hotels on their islands to buttress their claims. Vietnam has asked U.S. firms to explore for oil around the islands it occupies. Still, with China growing, its intentions uncertain, and its growth a source of wealth to all, no one in Southeast Asia is anxious to stir the pot too much.

The time factor may also explain China's resistance to Indonesian efforts to internationalize the Spratlys discussion. Its neighbors understandably see Beijing's insistence that the dispute must be settled by claimants alone as an attempt to prevent them from seeking help while China's position in bilateral negotiations grows ever more formidable.

Too Big to Handle?

Some Southeast Asians are, in fact, seeking help from the United States. Vietnam's contracts with U.S. oil firms suggest a subtle effort to involve the U.S. government in its Spratlys dispute. President Ramos of the Philippines has been more direct, arguing that the U.S.-Philippines mutual security treaty commits U.S. forces to defend his country's island claims. Others are ambivalent about U.S. help. Yet all are likely to take the U.S. response to more assertive Chinese actions as a litmus test of U.S. resolve and commitment to their security.

Thus far the United States has demurred, rejecting Ramos's treaty interpretation and warning U.S. firms that they explore disputed areas at their own risk. U.S. diplomats repeat endlessly that "no one should use force" to resolve these issues. With North Korea's nuclear program, Japan's security debate, and a host of trade issues crowding their East Asian agenda, U.S. policymakers understandably want to stay clear of a local dispute over tiny, desolate, and often submerged atolls.

Yet clearly the Spratlys dispute could threaten U.S. interests in a stable, open, and peaceful East Asia. The worst case, as recently described by Mark Valencia of the East-West Center, would be more frequent and violent clashes that could endanger shipping and eventually involve the United States or Japan. More likely but only slightly less worrisome

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would be continued stalemate, increasing tension, and the gradual emergence of an arms race around the South China Sea.

More broadly, growing Chinese assertiveness and military strength could strengthen hawks in Japan's ongoing security debate, in turn raising tensions among Japan's neighbors. And a souring of Sino-Russian relations could encourage Moscow to refurbish its nuclear doctrine, imperiling the arms control agreements fashioned as the Cold War ended. A growing China can threaten U.S. interests even if it means to threaten no one, and long before it can threaten the United States directly.

The United States is already involved in handling the effects of China's growth through its security ties to Japan and South Korea. It may become more deeply embroiled sooner than it thinks, for East Asians are unlikely to be able to handle these problems by themselves. For most East Asians, China is simply too big to handle alone; even the Russians feel vulnerable. Although China's neighbors might band together to balance China's power, especially now, with China still relatively underdeveloped, regional security cooperation is also underdeveloped. Deep underlying suspicions hamper cooperation in Northeast Asia, where close U.S. allies like Japan and South Korea prefer dealing with the United States to dealing with each other.

The Southeast Asians have ASEAN (the Association of Southeast Asian Nations, embracing Indonesia, Singapore, Thailand, Malaysia, the Philippines, and Brunei), which, since its founding in 1967, has gradually expanded both the range of issues it can discuss and the outsiders it includes. But the expansion process has been painfully slow and could easily fail to keep up with serious regional security problems. Besides, ASEAN scarcely controls the major power relationships around it. Its members work to keep the United States engaged in the region partly to sustain a stable balance within which they can operate with some freedom.

The United States and a Strong China

The possibility that the United States will be pulled into regional disputes involving China suggests a compelling need to collect the fragments of U.S. China policy—the concern for trade one day, arms transfers the next, help with North Korea the next—into a more coherent whole. The difficulty of predicting China's future is no excuse for ignoring the implications of China's continued growth.

The challenge is especially great since the United States, despite its own strength, has been consistently uncomfortable with the prospect of a strong China. This was true even during the Cold War, when China helped the United States counter Soviet power. A communist power, indirectly a recent enemy in Vietnam, and a direct threat to Taiwan, China was not the most cooperative of strategic partners. Beijing resented U.S. support to Taiwan, feared U.S. inconsistency, and

was reluctant to curtail its own freedom of action by tying itself closely to the United States. After 1982 each country tended to go its own way, China to a more balanced stance between the superpowers, the United States to a more Japan-oriented anti-Soviet policy.

As the need for strategic cooperation declined, tensions in the relationship began to rise. Some had to do with China's internal behavior, notably its human rights abuses. But others—concern about the growing U.S. trade deficit with China, for example, or about China's arms sales to unsavory Middle Eastern regimes—were grounded in skepticism about the kind of international citizen China intended to be.

Even the human rights debate, so prominent after the Tiananmen crackdown in 1989, was not without strategic content. Those wishing to curtail China's most-favored-nation (MFN) trade status with the United States were saying, in effect, either that the United States should not help China grow strong or that it should help only if China's behavior met certain standards. Some continued to define those standards in terms of China's international behavior—its arms transfers and trade surplus. But even those most concerned with human rights expected a more democratic China to be better behaved internationally.

The human rights-trade link was based partly on the assumption that, with the Cold War over, China was weak and strategically unimportant; with strategic allies, after all, Washington handles human rights issues quietly and behind the scenes. Whether that assumption was true at the time (the Soviet Union's collapse actually increased China's regional power by removing a threat), it isn't now, as President Clinton's recent move to sever the link suggests. If the United States wants to deal with a growing China, it will have to refine its tools for doing so.

China and Arms Control

Indeed, it will have to drop more than the "sledgehammer" of curtailing China's trade status. Long before they raised this threat, U.S. policymakers sought to induce China's adherence to various global arms control agreements by offering or refusing to license the export of U.S. high technology, in effect offering to help China grow strong so long as it agreed to play by established rules of "good" state behavior. The effort never worked that well and is probably outrunning its usefulness.

To be sure, China has slowly become more involved in arms control. In 1980 it sent its first delegation to the disarmament conference in Geneva,



where its negotiators have become increasingly involved in shaping agreements like the Chemical Weapons Convention and the Comprehensive Test Ban Treaty. Nor has China been completely unwilling to sign certain agreements—especially those that constrain others besides itself. Thus it signed the Outer Space Treaty in 1984 to slow a superpower “space race” that might have degraded its nuclear forces. But it has refused to negotiate nuclear arms control, since to do so might ultimately hobble its top-priority but still relatively underdeveloped nuclear weapons program.

Problems arise for the United States in the range of agreements that lie between the easy and the unacceptable. The Non-Proliferation Treaty (NPT) and the Missile Technology Control Regime (MTCR) would cut China’s lucrative sales of nuclear and missile technology and marginally curtail its ability to support old allies (Pakistan) and new friends (Iran, Syria). Here U.S. technological inducements have affected China’s commitment to arms control. But they have had less effect on China’s behavior.

China finally joined the International Atomic Energy Agency in 1984 to gain access to U.S. commercial nuclear power technology then being denied by a Congress deeply suspicious of China’s attitude toward proliferation. Although China did not then join the NPT, its leaders stated publicly that they would not engage in nuclear proliferation, and privately that they would not help Pakistan’s nuclear weapons program. According to U.S. intelligence reports, however, they continued to do precisely that. When Beijing finally joined the NPT in 1992, again in return for U.S. high-tech sales and also in response to world outrage about the post-Desert Storm exposure of Iraq’s massive clandestine nuclear weapons program, reports of illicit sales to Pakistan continued.

A similar pattern of halting entry and spotty compliance has marked China’s acceptance of the MTCR, to which Beijing committed itself late in 1991 as part of the same high-tech deal that brought it into the NPT. China reportedly canceled prospective missile sales to Syria and Iran. But evidence of continuing Chinese missile technology exports to Pakistan forced President Clinton to invoke U.S. sanctions in August 1993.

Some would not hold Beijing responsible for illicit arms sales, arguing that the sales are often conducted by relatives of China’s ruling elite, who operate beyond the control of the Foreign Ministry. Yet precisely

because they are related to China’s rulers, these operators could presumably be brought to heel if those rulers cared enough to do so.

At the other extreme are critics who see Beijing as a rogue state that, in the words of Senate staffer William Triplett, “has violated every nonproliferation pledge it has ever made” Yet this charge, while partially true, overlooks the distance Beijing has come—from revolutionary power opposed to arms control to a “semi-status-quo” power that has signed several arms control agreements and complies with some, if not all, of them. Unless we write cases of compliance off as deception (which some do—this is, after all a civilization for which deception is a key strategic virtue), there is more of a puzzle here than China’s critics admit.

Established Power, Growing Power

Perhaps tensions between the United States and China on arms control are only to be expected. The established rules of international conduct, written by the strong and naturally favoring their interests, are likely to be resented by *any* rising power. Thus the NPT freezes nuclear inequality in place, and any nuclear arms control talks would also likely assure China’s current inferiority. And the MTCR forbids missile sales (among China’s few marketable military technologies) while leaving U.S. aerospace firms free to market sophisticated aircraft worldwide.

Small and weak states, destined always to be rule takers rather than rule makers, may have to accept this situation and satisfy their interests as best they can. By contrast, rising powers, especially one with China’s proud past, recent growth rates, and enormous potential, have every reason to resist agreements that reflect current power relationships in hopes of negotiating from a stronger position down the road. This seems to be Beijing’s approach to the Spratlys.

But the United States is too powerful and potentially dangerous to be put off. Besides, its technological inducements have been useful. And if some of the rules the United States proffers appear unfair to the Chinese, others may be growing more attractive as economic growth increases China’s stake in the prevailing status quo. China’s spotty record of compliance with arms control may reflect the ambiguities of this situation.

But cheating has also been a form of power—a risky one, but perhaps the only one available to China at its current stage of development. Take China’s illicit links to Pakistan. Rather than vehemently denying accusations that it continues to sell missile components to Pakistan, Beijing has instead offered to discuss those sales if the United States will discuss its 1992 decision to sell F-16s to Taiwan. Evidently the Clinton administration has recently agreed to this linkage. Cheating has opened the chance for leverage over a weapons deal China staunchly opposes.

For now, U.S. officials will do no more than listen



politely but then ignore China's arguments, as they have in the past. But past practice may have a limited future, since the stakes in this game are changing in China's favor. Growth and global involvement are reducing China's need for U.S. technology, while the collapse of the Soviet Union has reduced the urgency of China's search for technical advance. For the United States, on the other hand, the end of the Cold War has made proliferation more worrisome than ever. It will be increasingly difficult to "buy" China's agreement with dribs and drabs of U.S. technology. As is the case with the F-16 sale, China will want U.S. strategic concessions in return for concessions of its own.

Which raises the larger issue at stake here. China's argument that missiles and sophisticated strike aircraft are equally dangerous and ought to be jointly controlled—a position that may well be analytically valid—was excluded from the MTCR talks in the interest of simplicity and practicality. In forging a link between its missile sales and the U.S. F-16 sale to Taiwan, Beijing is forcing its broader argument back onto the agenda. To the extent that it succeeds, it will be leaving the realm of rule-takers and entering the world of rule-makers.

The United States has been willing to see China help write rules that play to U.S. interests, like the Chemical Weapons Convention. But is it ready for such help on subjects dear to its heart? Is it ready to curb its own arms sales, now far and away the world's largest and a key source of income for the shrinking U.S. defense industrial base, in return for curbs on China's? Is it ready to limit the size, type, or operational freedom of its own forces in East Asia in return for limits on China's force modernization? These questions are far fetched now, but perhaps not for long.

Rules or Power?

Obviously ambitious strategic agreements are worse than useless if Beijing cannot be trusted to keep its word. But that argument goes both ways. China's leaders regard the U.S. F-16 sale to Taiwan as a violation of the 1982 U.S.-China Communiqué on Taiwan, by which Beijing *thought* it had gained limits on such sales. In fact, the United States has consistently reinterpreted the Communiqué to suit the needs of Taiwan's defense, hungry U.S. defense firms, or presidents campaigning for reelection. A recent Senate move to elevate the Taiwan Relations Act above the Communiqué, virtually nullifying the latter, was softened only by last-minute executive branch lobbying. Surely if the United States can tailor its understanding of signed agreements to its loyalty to an old ally, Beijing can tailor its reading of the MTCR to its continued support to Pakistan?

Despite expressions of outrage over the F-16 sale, China's leaders were not surprised by the move. Strong states, they know, do what they will, while weak states do what they must. Behind moralizing

U.S. rhetoric they see a state that does what it will, fashioning agreements to suit its interests and reinterpreting them when convenient. China's leaders take a realpolitik view of the world. No doubt they will "do what they will" if and as their country grows more powerful. Meanwhile, they have every incentive to justify their own arbitrariness by referring to U.S. behavior.

Again, the immediate issue is Taiwan; China's continued growth will make it increasingly difficult for the United States to sustain the studied ambiguities of its policies toward Taiwan and the People's Republic. And the general point applies across the range of activities where U.S. and Chinese interests potentially collide. If U.S. officials want to ground U.S. relations with China in rules—whether tacit or codified in elaborate agreements—they are going to have to abide more honestly by rules themselves. Beijing will happily be a mirror, reflecting U.S. misbehavior in its actions, with penalties that grow as China grows.

Balancing and Bargaining

China may misbehave anyway; treating it more equitably only maximizes the prospects that it will not. Thus until we know a great deal more about China than we do today, the complement to a more equitable U.S. approach to the country will be continued U.S. strategic engagement in East Asia and vigilance over China's actions. Whether China chooses to become the expansionist dragon some expect or instead seeks the cooperative relationship with the United States that China's leaders say they want, the currency of the relationship will be power, and that means the United States had best keep a good deal of it on hand. If China's leaders conclude that the U.S. military is leaving East Asia in any case, why should they take the United States any more seriously than the United States now takes them?

Ironically, if the challenge to Americans today is merely to think of China as a potential equal, should China actually exploit its raw potential, Americans will find themselves challenged merely to maintain equality! That day may never come (perhaps the sheer enormity of the prospect helps explain why many Americans hope it does not). But economic growth and changed strategic circumstances have already made China's increasing power a potential threat to U.S. interests. It is time Americans began to adjust their policies, and more importantly their perspectives, to prepare for the possibility of a China stronger than any they have seen before. ■

IS THE UNITED STATES

READY TO CURB

ITS ARMS SALES IN

RETURN FOR CURBS

ON CHINA'S?

INDUSTRIAL SEA CHANGE

How Changes in Keiretsu Are Opening the Japanese Market

KEIRETSU. Americans have spilled much ink trying to come to grips with the cooperative business structure that links Japanese companies into industrial groups and that, Americans widely believe, keeps U.S. companies out of the Japanese market. Many strategies have been proposed to combat keiretsu—from using Japanese antitrust enforcement to break up monopolistic transactions among members of industrial groups to forcing Japan's government to loosen restrictions against U.S.-style mergers and acquisitions with which to oppose them. So far, however, none of these strategies has been very successful. The penetration of foreign manufacturers in the Japanese market remains low.

It is time to try a different approach. Over the past decade the keiretsu relationship has been undergoing changes, and those changes offer an expanded opportunity to gain entry into the Japanese markets.

The Changing Keiretsu Relationship

The heart of the keiretsu relationship has been the affinity of Japan's business culture, both corporate managers and employees, for long-term cooperative relationships. Traditionally Japanese managers have opted for long-term contracts with a limited number of partners. Employees have favored a system of lifetime employment. And the two sets of preferences have reinforced each other.

Throughout the post-World War II era, the managers of Japan's largest companies have kept their companies slim, preferring to contract large amounts of labor-intensive work out to smaller firms rather than to absorb new contracts through mergers and acquisitions, as many U.S. managers have done. One reason large Japanese companies began contracting work out was the substantial wage difference between large and small companies: in 1960 salaries in small firms were only about 60 percent of those in large firms. Another was the need to finance every new employee po-

sition for the jobholder's lifetime. Managers who know they are expected to keep employees on the payroll until retirement are particularly cautious about hiring more workers.

Other characteristics of the keiretsu relationship, from cross-shareholding among partner companies and their banks to the kanban system of just-in-time delivery, with the manufacturer depending on its supplier to furnish inventory as needed, also knit keiretsu member companies together in long-term cooperative relationships.

Lately, however, the rationale of the keiretsu system has begun to weaken. First, dealings between contractors and subcontractors have been strained by purchase practices that subcontractors find objectionable. Some subcontractors, for example, especially in the service and retail industries, must do their work on extremely short notice and at quite low fee rates. In addition, with the Japanese economy in recession and industry no longer expanding, subcontracting companies have been unable to depend on the traditional single long-term relationship. In 1986, when a sudden appreciation of the yen slowed the Japanese economy, even Toyota advised its subcontractors to build up business with other contractors.

The perspective of employees is also changing. Well-educated workers, especially women, are beginning to have second thoughts about the lifetime employment system, viewing it less as a source of social status and more as an impediment to their self-development as professionals who might want a variety of business experience.

Shrinking wage differences between large and small companies (salaries in small firms are now nearly 80 percent of those in large firms) have erased much of the cost advantages of keiretsu relationships for managers of larger firms.

Even the just-in-time delivery system has recently come under fire. Although the frequent deliveries of parts are useful for manufacturers, they worsen traffic congestion and impose onerous work schedules on the suppliers.

These changes in the value of the keiretsu relationship offer American companies a way to break into the Japanese

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market. Americans may, for example, be able to negotiate subcontracts with suppliers of high-quality goods or services who are seeking multiple long-term relationships with companies outside the old keiretsus. They will be able to hire workers who already have substantial work experience in Japan and want to change their careers. Mobil Sekiyu, the second largest foreign petroleum company in Japan, is already trying to attract talented workers by offering high-quality employee training, promoting women aggressively, and improving working conditions.

U.S. companies can use these strategies to establish a substantial base in the Japanese economy and then penetrate the institutional barriers of the Japanese industrial system through offering cooperation in newly emerging technologies and product development—areas in which even the older large companies that dominated the keiretsu system are less effective.

Changes in Financing

Even more important to U.S. business are major changes in the system of financing used within the keiretsu structure. Just after World War II, Japanese business, having no significant capital to invest, had no choice but to borrow money. Financial markets were immature, and the government encouraged banks to be the primary intermediaries between savers and investors and to set interest rates low to enable businesses to borrow money.

Beginning in the early 1970s, Japanese managers began to derive more of their funds directly from the bond and equity market. Yamaha, a large musical instrument, motorcycle, and sports equipment company, issued new stock at the market price for the first time in Japan in 1969. Over time the debt-equity ratio of domestic companies gradually fell, from an average of more than 70 percent in the 1950s to under 50 percent in the 1980s. Their dependency on the banks has declined even further.

Still, bank loans continued to play an important role in financing, with three factors leading companies to continue to borrow. First, interest rates remained low. Second, government restrictions in the financial sector slowed the development of the bond, commercial paper, and asset-backed securities markets. Finally, newly accumulated equity was often used as collateral for new loans. When a keiretsu member asked the group's main bank to purchase its newly issued stock, the bank almost invariably asked it to borrow money in return, using some of its increased capital as collateral. But despite the continued reliance on borrowing, in fact the primary role of banks has changed—from one in which they lend money to their group companies to one in which they hold newly issued stock.

Cross-Shareholding: A Core of Keiretsu?

At the close of World War II cross-shareholding among related businesses offered a way to absorb liquidated stocks (resulting from the breakup of

major Japanese prewar holding companies) that the market could not otherwise have handled. It also helped protect Japanese companies from takeovers by foreign investors or companies. It can still serve that purpose—and did in 1984, when members of the Mitsubishi Group protected the Mitsubishi Oil Company from being acquired by Texaco.

As a result of cross-shareholding, banks hold more than 40 percent of all stock listed on all Japanese stock exchanges, other companies 30 percent, and individuals only a little more than 20 percent.

But cross-shareholding, too, has begun to change. In particular there is less cross-shareholding within keiretsu groups. Keiretsu member companies have begun seeking transactions with companies outside the group. In 1989 Nikkei Newspaper reported that five Japanese companies, all unconnected, made cross-shareholding arrangements for reasons of business strategy and access to new technologies, not historical ties. As Kenicki Imai, of Stanford University, has noted, “technological and engineering perspectives,” rather than keiretsu relationships, are increasingly determining interfirm linkages. Finally, cross-shareholding purely for the purpose of providing finance rather than corporate control has increased since the 1980s.

Why Is It Easy to Issue New Stock in Japan?

In the United States, stockholders traditionally oppose plans to issue new stocks to a third party because stock prices generally fall as a result. By contrast, Japanese companies can, and often do, choose to issue new stock—and the price of their stock often *increases* after the new shares are made available. The explanation for the sharply different experience in Japan is twofold: the price-earnings ratio of Japanese companies is quite high, and dividends are extremely low. When stock prices are high, a company can raise a considerable amount of money by issuing a small amount of new stock. Yet a low dividend pay-out implies only a negligible increase in future cash payments. Thus the cost of issuing new stock is often lower than interest rates for loans. These conditions, however, seldom happen in the United States, where high dividend rates and relatively low price-earnings ratios make the cost of issuing new stocks the same as, or higher than, interest rates for loans.

Why do Japanese stockholders accept such low dividends? The answer used to be that Japanese companies preferred participating in the keiretsu cross-shareholding system over receiving and paying a higher dividend. But increasingly the answer is that domestic companies that create new cross-shareholding networks can mutually increase the potential value of their assets by issuing new stock and then borrow money cheaply by using these stock assets as collateral for new loans. The Japanese accounting system, which for tax purposes does not require companies to change their balance sheets in accordance with the increase in the “hidden value of assets” (the difference be-

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tween book value and actual market value), also undergirds the system.

Recession and the Financing System

During 1987–90, the period of Japan's "bubble economy," most of the major Japanese companies engaged in aggressive equity financing and built strong cross-shareholding relationships with main banks.

These business strategies, however, were abandoned abruptly in 1990, in the aftermath of several huge downturns in the Japanese stock market. The consequences for both Japanese banks and corporations in the early 1990s were severe. Large banks and insurance companies suffered as the hidden asset values on which they had relied heavily for expanding their businesses fell sharply. Most major companies' operational profits fell dramatically during the severe economic recession that began in 1991. And since 1992 companies have been obsessed with redeeming convertible bonds that they had issued during the bubble economy and that have not been converted to stocks.

All this is further straining the keiretsu system. No longer able to rely on the old certainty that stock prices would be going up, Japanese companies and banks are far less willing than before to hold stock in keiretsu-member companies. The volatile state of the Japanese stock market has driven off most substantial purchasers. Even if some companies wanted to issue new stocks, there is no one to buy them.

This situation, painful as it is for Japanese companies, offers U.S. business an important opening into the Japanese market. Although some economists believe that the Japanese cross-shareholding financial system collapsed completely with the end of the bubble economy, the conditions in Japan's stock market that encouraged equity financing and cross-shareholding have not changed substantially: equity prices remain relatively high, and dividends, extremely low. Most notably, because stock prices have not dropped as dramatically as average company profits, the average price-earnings ratio has increased nearly to 80 (compared with about 25 in the United States).

How Can U.S. Companies Invest in Japan?

Despite its unique nature over the postwar period, the Japanese business system, especially its financial component, will not be able to remain isolated from U.S. or European systems permanently. Japan's traditional financial system is under pressure on many different sides.

For example, although the continuous asset price increase (gradual at first, and then dramatic during the bubble economy) nurtured by the postwar financing system has contributed to the rapid progress of Japan's economy, it has also kept Japan's people from being able to buy property—a state of affairs that Japanese appear less and less willing to tolerate.

And given the current strains on the keiretsu system, Japanese banks and stock companies will

surely begin developing international risk management methods independent from the other keiretsu members.

In addition, recent amendments to Japanese commercial law have made it easier for stockholders to sue their company, a change that may encourage company managers to increase dividends in accordance with their profits.

Finally, capital standards set by the Bank for International Settlement (BIS), which are supposed to be strengthened further in the near future, may prevent Japanese banks from holding large amounts of equities in their asset portfolio.

But the adjustment of the Japanese financial system to the international financing systems will be gradual, and in the interval elements of the old keiretsu-style financing structures will continue to operate, particularly as long as the two key stock market conditions (high price-earnings ratio and low dividends) remain.

The gradual weakening of both the keiretsu relationship and the cross-shareholding systems offers U.S. companies opportunities to use equity financing of the sort that boosted industrial growth in Japan. They can even establish temporary cross-shareholding relationships with Japanese companies for the purpose of arranging efficient financing. A Japanese company issuing new stock in the domestic market and a U.S. company issuing convertible bonds in the Euro-market could enter a cross-shareholding arrangement to increase their respective potential assets. They could also use these assets as collateral for new loans, as the big Japanese companies did before the bubble economy. U.S. companies can pursue these strategies because, not having previously acquired substantial stocks and property in the Japanese market, they, unlike many Japanese keiretsu companies, have not been hit by the decrease in the value of these hidden assets.

I do not mean to suggest that U.S. companies should always follow Japanese business methods when they operate in Japan. They can protest Japanese business structures they think unfair. But at the same time, they should take advantage of the current business opportunities, particularly those related to financing.

Now is a turning point for the Japanese economy. Since World War II the keiretsu-style cross-shareholding system and the hidden assets of property and stocks have been the chief risk absorbers in corporate and financial management. But from now on, Japan must rely more on strict risk-management financing and operating systems, which can no longer be guaranteed by the keiretsu membership ties. Success in this reform will help create Japan's future prosperity—a prosperity it will enjoy under a more mobile system of labor management, a more deregulated financial market, and a simpler distribution system. Farsighted U.S. companies will invest in the Japanese market now—a move the highly appreciated yen has made harder, but not impossible. ■

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“ H O L L O W ”

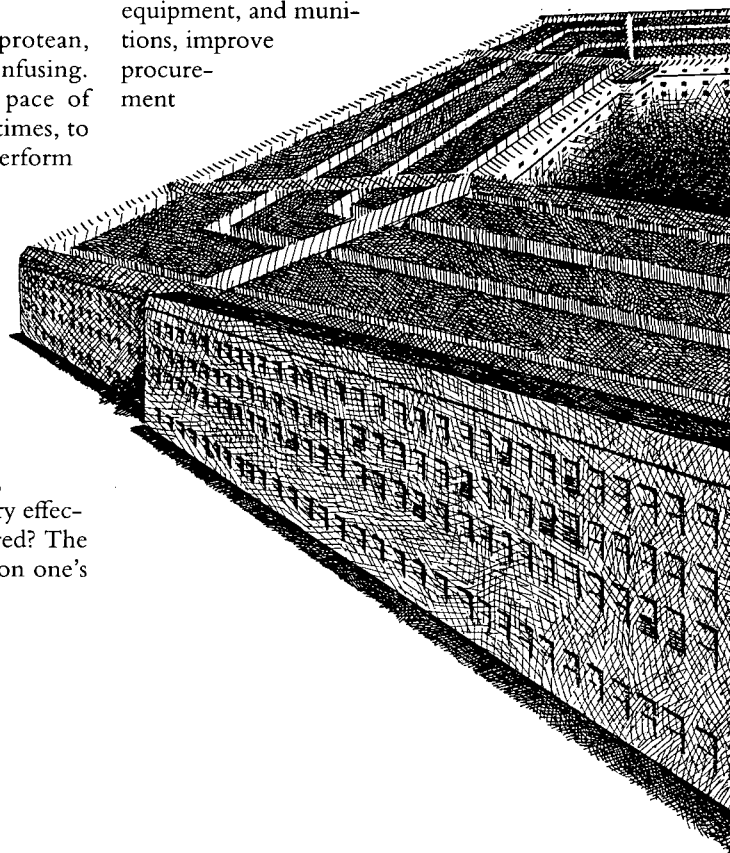
Recent fears expressed by Senator John McCain (R-AZ) and others about dramatic declines in the readiness of U.S. military forces echo concerns voiced widely toward the end of the 1970s. At that time, apprehensions about America's “hollow force” centered on the readiness of existing military capabilities—illustrated most dramatically by the mechanical failures that led to the aborting of the 1980 attempt to rescue American hostages in Iran. Today McCain's charge that American forces “are going hollow” does not so much concern personnel or system readiness as it does the issue of whether America's overall military forces are too small—and thus inadequate to provide for the nation's security needs.

The term “readiness” has always been protean, and thus discussions about it potentially confusing. Sometimes readiness refers simply to the pace of training in tanks, planes, and ships; at other times, to the ability of forces to deploy quickly and perform initially as designed to do; at still others, it means something more like effectiveness against a specific enemy in achieving a specified objective such as an unconditional surrender. For purposes of the current debate about readiness, the broader definition—military effectiveness—seems to catch the essential concern.

Elements of Effectiveness

Defining readiness as effectiveness, however, raises other questions: what determines military effectiveness and how can effectiveness be measured? The answer to the first question depends in part on one's

time frame. In the short term, over a period of a few years, it may be possible to alter effectiveness by changing strategic concept (does security entail thinking in terms of two wars or one? nuclear or conventional? stalemate or “victory”?), the rate at which forces are reduced (but not increased, which takes a lot of time), operational tempo, training, and stocks of munitions and secondary items of supply. As Senator McCain has pointed out, in the six months of Desert Shield leading up to Desert Storm, it was possible to draw on forces not originally included in Central Command's contingency plans because no other plausible military threat existed. Desert Storm planners were able to modify training, equipment, and munitions, improve procurement



Current Issues of U.S. Military Readiness and Effectiveness

FORCES?

and logistical systems, even mobilize and deploy elements of the National Guard and Reserve.

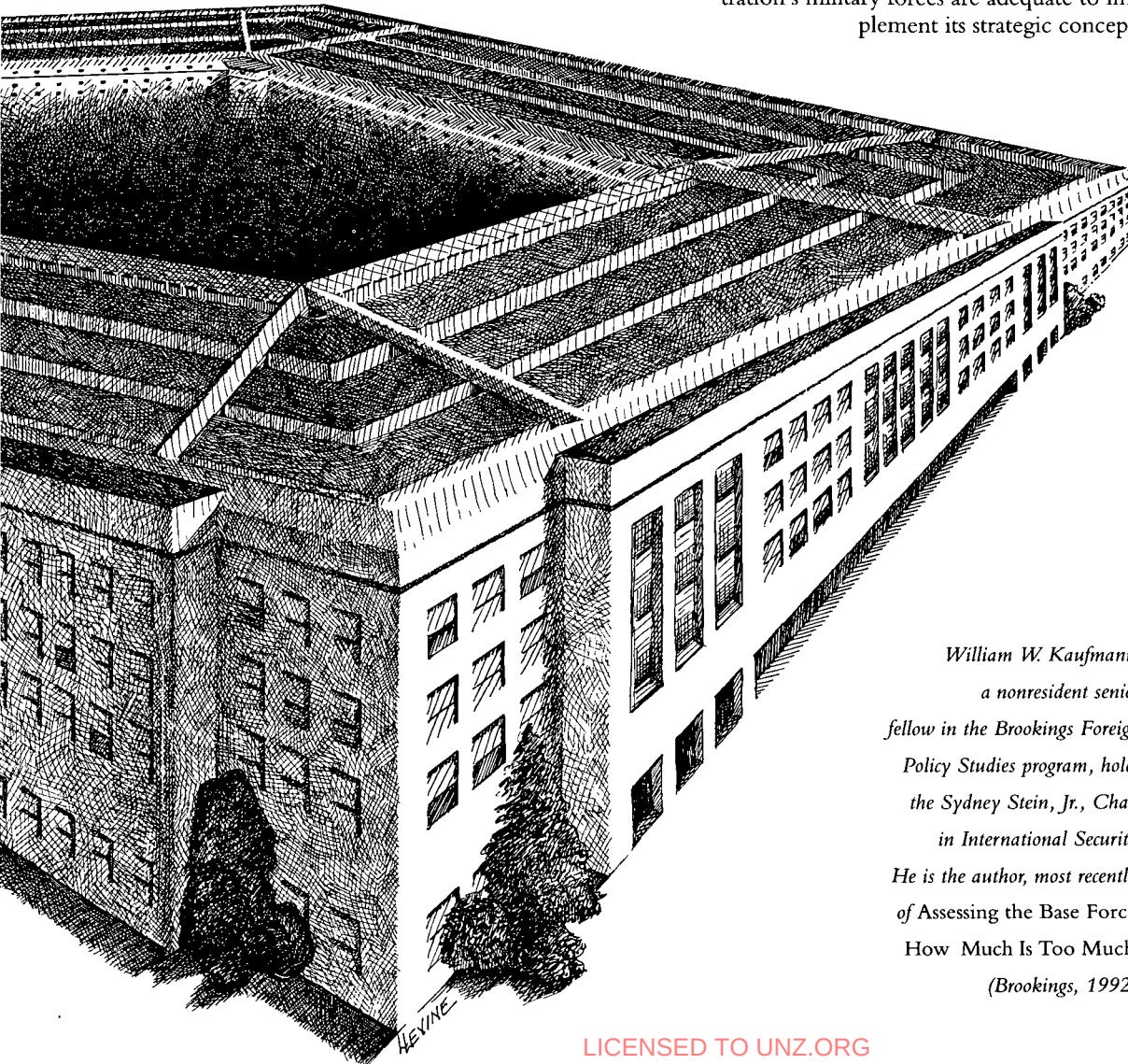
But many key determinants of effectiveness cannot be changed in the short run. Among the stickier elements are force size and composition (unless the training and callup of reserve ground combat units can be improved quickly). Replacing current with next-generation weapons, equipment, and munitions takes time. So do big increases in airlift and sealift, especially if the added units must satisfy military specifications as to weight and size of equipment and

rates at which it is unloaded in congested ports or over beaches. In other words, decisions made today about long lead-time items such as ships, submarines, aircraft, ballistic missiles, tanks, and (increasingly) well-trained personnel not only in the United States, but also in other countries, will affect performance and outcome many years hence. Accordingly, the Defense Department must always balance short-run against longer-term considerations.

Current Issues: Forces and Strategy

The current debate about readiness focuses on two such issues. The first is whether the Clinton administration's military forces are adequate to implement its strategic concept.

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(Brookings, 1992).*

For all practical purposes, the strategic concepts used by the Bush and Clinton administrations are identical: both assume two virtually simultaneous wars, one starting in the Middle East, to be followed shortly by another on the Korean peninsula, and both require that U.S. and any allied forces effectively demolish opposing military capabilities. But Clinton's "Bottom-Up Review" requirements for the two contingencies are somewhat more modest than those of Bush's Base Force. Because the Clinton administration announced its future-years budget plan for defense before it even commissioned the Bottom-Up Review, however, it should surprise no one that questions have arisen about both. How could it be that in 1992 the Defense Department said it needed 15 active-duty divisions (12 Army and 3 Marine Corps) as well as 26 Air Force fighter wings (15 active and 11 reserve) when only a year or so later the same department said it required only 13 active-duty divisions (10 Army and 3 Marine Corps) along with 20 Air Force fighter wings (13 active and 7 reserve) for the same planning contingencies and expected outcomes? For many observers, indeed, the Base Force was more appropriate than the Bottom-Up Review Force both in size and composition and in cost.

In fact, relatively straightforward calculations and variations in the combat power and effectiveness of the belligerents suggest that both the Bush and Clinton forces are pretty much on the flat of the effectiveness curve, especially where nuclear warheads, ground forces, and carrier battle groups are concerned.

To put the matter another way, smaller U.S. forces on the ground, but larger Air Force tactical fighters than are programmed by the Bottom-Up Review, combined with fewer carrier battle groups, would achieve virtually the same results as the Base or Bottom-Up Review Forces—and at significantly lower cost. Since the future defense budgets were set before the analyses, planners could afford to be very conservative, pick extremely pessimistic scenarios, and ignore the law of diminishing returns to scale.

Current Issues: Future Funding

The second question in the current readiness debate is whether the Bottom-Up Review Force, or for that matter the Base Force, will be adequately funded through the latter part of the century, assuming their ability to reach specified strategic objectives. By fiscal year 1999, for example, the Clinton administration has estimated that the Base Force would cost about \$246 billion (in 1995 dollars), the Bottom-Up Review Force, only \$227 billion, or \$19 billion less. In reality, both will probably cost much more.

There are two reasons why larger defense budgets are likely to be the wave of the future, absent a further review of potential threats and U.S. defense needs. First, budget authority for military procurement has dropped from \$132 billion (in 1995 dollars) for fiscal year 1985 to about \$43 billion for 1995, a cut of nearly \$89 billion, or more than 67 percent. By contrast, the military personnel account has gone down 24 percent; operations and maintenance, only 10 percent.

The dramatic drop in procurement dollars was

made possible by enormous increases in the procurement account between fiscal 1982 and 1991. During those 10 years, Congress appropriated more than a trillion dollars (in 1995 dollars) for procurement alone. As a consequence, accumulating balances of prior-year budget authority, mostly for procurement, amounted to \$218.5 billion as late as the end of fiscal year 1993. Of that total, more than 75 percent was obligated—earmarked for specific purchases. But nearly 25 percent, or \$53.6 billion, remained unobligated and was available to fund previously authorized contracts. In other words, as far as procurement is concerned, the Defense Department is still living off the largesse of the 1980s and can afford to keep its procurement budget low (although outlays continue to outpace budget authority).

The prior-year balances are now going down and could fall even lower if Congress rescinds some of the unobligated authority. Eventually, procurement appropriations are bound to increase if the size of the Bottom-Up Review Force (or the Base Force) is maintained. How much these appropriations increase will naturally depend on many things, including decisions about how to modernize the forces.

The second reason defense costs are likely to rise by the turn of the century—despite a number of system cancellations and stretchouts—is related to the first. The sharp drop in appropriations for procurement enabled the Defense Department to retain larger forces than it would have if procurement had returned to the historical level of approximately 27 percent—instead of the current 17 percent—of the annual defense budget.

This situation cannot last. If modernization is to proceed, whether by buying current systems and upgrades or by selectively acquiring more expensive next-generation systems; if readiness, as measured by the size of the Operation and Maintenance account, is to be kept high; and if the age of the force is to be kept low, both nuclear and nonnuclear forces will almost certainly have to be cut further—to the point, say critics, that the United States would be left outmanned and outgunned by potential enemies.

That is one possibility. Another is that if the administration and Congress decide to stick with the Clinton goal of a defense budget in the neighborhood of \$227 billion by century's end, the reductions in force can be quite small. The START II goal of reducing total U.S. nuclear warheads to 3,500 by fiscal year 2003 is much too conservative. With Russian reciprocity and U.S. aid, warheads could fall to 1,500 on both sides, with the retired systems effectively disabled by 1999. In this esoteric realm, at least, reduced readiness could be seen as a boon to Russia as well as the United States.

On the nonnuclear front, retaining 11 carrier battle groups on active duty (and one in reserve) lacks any serious military justification. A stripped-down force of nine (with fewer expensive escorts) would serve just as well. For the Navy can substitute ships other than carriers on station in the Mediterranean, the Indian Ocean, and the Pacific, if that should even prove worthwhile as compared with periodic sorties in force.

Savings in these two areas alone would support a major program of modernization with current-gener-

ation systems and a robust investment in research, development, test, and evaluation. The upshot could well be a more ready and effective force by the end of the century than the one now programmed by the Clinton administration.

The Desert Storm Equivalent

Another issue that bears on future readiness is whether Desert Storm provides a suitable model for force planning. It may, indeed, be appropriate to use Iraq or Iran and North Korea as conceivable enemies and sudden attacks by them as the most demanding contingencies of the next decade or so. But, as noted, the planners of Desert Storm could draw on virtually the entire U.S. nonnuclear arsenal for the campaign, despite the existing two-war strategic concept, and more carrier battle groups and divisions were deployed than proved necessary for the stunning success of the United States and its allies. This is not to criticize the planners of Desert Storm. The forces were available, so why not deploy them? But there is no reason to assume that, with only slight modifications, a Desert Storm equivalent is essential for any serious regional contingency. The claim that future threats in the Middle East and Northeast Asia will require 10 Army divisions, 3 Marine divisions with their air wings, 11 or 12 carrier battle groups, 200 heavy bombers, and 20 Air Force fighter wings may be politically correct. But the warfighting assumptions behind the Bottom-Up Review remain to be revealed. Meanwhile, smaller forces, better balanced between investment on the one hand and operating and support on the other, appear to be almost equally effective and would be a good deal cheaper.

Measures of Effectiveness

The above assertion suggests a critical hypothesis: that we can learn to measure, monitor, and foretell, with modest accuracy, effectiveness in the longer run as well as in the shorter term. We can do so, however, only provided that we consider specific opponents in specific environments and that we define outcomes in measurable terms. It is one thing to talk about Iraq equivalents or generic enemies with a range of capabilities. It is quite another to analyze a conflict with North Korea not only on the Korean peninsula (where South Korean troops mass behind elaborate fortifications), but also in an international context that includes the United Nations and other powers such as Russia and China, all of whom could help prevent a conflict.

Although some reject such analytic efforts as presumptuous, in fact we are already making them in one form or another. When General Schwarzkopf is alleged to have wanted a three-to-one advantage over Iraqi forces, he was predicting that with such an advantage, he would be able to defeat Saddam Hussein. When then-Congressman Les Aspin used publicly available measures of combat power, originally developed for the Army, to rate North Korea as only 60 percent of prewar Iraq in air and land combat potential, and projected how much the United States would need to reinforce South Korea (not much), he

Larger defense budgets are likely

to be the wave of the future,

absent a further review of potential

threats and U.S. defense needs.

**The proper responsibility of the
Defense Department is to advise both
branches of government as to what
they can buy in the way of capability
at various levels of investment.**

was not only engaging in force planning; he was also forecasting a Desert Storm-style victory as a consequence of these calculations.

In any projection of effectiveness, obviously, the potential enemy, where he is located, and what combat power and destructiveness he might bring to bear against the United States and its allies are key factors. So is the type of war that might be hypothesized, whether nuclear or conventional—or even unconventional as was partly the case in Vietnam and Somalia and could be again in Bosnia.

In the nuclear realm, measures of effectiveness include targets destroyed and other types of damage inflicted, usually industry wrecked and people killed and wounded. Efforts to knock out the other side's nuclear capabilities have been studied, as have attempts to gain "meaningful superiority" and limit damage to the United States. Increasingly, however, these hypothetical exchanges have come to result in stalemates of cataclysmic proportions. Thus the main test of U.S. strategic nuclear effectiveness has come to be the ability of the offense to survive an enemy surprise attack and go on to destroy 80 percent or more of a large and diversified enemy target list. Never having fought a nuclear war, of course, we have no direct evidence of how our nuclear forces would actually perform, but it is, for the moment, difficult to dispute those calculations since the deterrent seems to have worked. (It is still possible that archival research may prove this conclusion wrong because no one intended to launch a nuclear attack in the first place.)

It is far easier to identify winners and losers in non-nuclear confrontations. Thus it remains possible to consider the prospect of favorable outcomes measured in destruction of enemy forces, the time taken to do so, the territory occupied (if that proves relevant), and the losses suffered by allied and U.S. forces. In the murky area of unconventional warfare, effectiveness usually entails some form of "pacification" measured in area controlled and by the "crime rate," combined with damage of the main force of the enemy and changes in the volume and reliability of information about the enemy.

Effectiveness and Costs

Measuring effectiveness by itself may help policymakers make choices about planning and committing forces. But if they are to know whether their choices are efficient, they must know not only the dollar cost of each unit of force, but also the annual operating and support costs of each. With that combination of data, they can then compare one set of programs or forces with another and also begin to see where constant increases in cost result in diminishing returns in effectiveness. To the extent that such relationships can be established, policymakers can decide at what point the increases in effectiveness are no longer worth the incremental cost.

Improving the Data

Determining the power of a nuclear warhead to do damage and the probability that it will destroy the

target is reasonably well documented. Measuring the amount of combat power and lethality of a U.S. mechanized infantry division relative to an enemy force is more complicated and the results less well documented.

Better data can be collected through carefully designed experiments under a variety of conditions as closely approximating combat as the safety of the participants permits. Outside of combat itself, the national training centers may provide the best sources of data, so it would make sense to add more main sites and satellites to the current system, as well as to undertake additional joint exercises. At a minimum, more data can be collected; better still, more units can be put to the test in a given period of time.

Actual combat data from recent conflicts also need to be reviewed, systematized, and aggregated to fit with analyses of cost and effectiveness and to permit replication. It would be useful, for example, to replicate—at a considerable level of aggregation—the results of Desert Storm and to see how sensitive those results are to changes in force size and composition.

Increasing and Diminishing Returns

If the data problem can be solved, it may become possible to replace rules of thumb, some quite antiquated, with more up-to-date measures based on increasing and diminishing returns to scale. Flight training hours, for example, are expensive in that they generate both direct and indirect costs such as fuel, maintenance, overhaul, spare parts, and replacements. The Air Force, presumably based on some measure of effectiveness, wants each of its active-duty fighters to fly 20 hours a month. Navy and Marine Corps tactical air and antisubmarine warfare units, on the other hand, are expected to fly 24 hours a month.

These numbers raise a host of questions. Is flying for the Navy and Marine Corps more demanding than for the Air Force? How much difference in cost and effectiveness would it make to add 4 hours a month to Air Force unit training? What would happen to Navy and Marine Corps tactical air effectiveness if their unit training fell to 20 hours a month? To 18 hours? Or rose to 26 hours? What would be the consequences of increasing the hours of training per day, but decreasing the number of days per month? How fast do pilots and crews lose their skills? Why is it that Air Force Guard and Reserve units fly roughly half the training hours of their active-duty counterparts, but frequently outperform them in competition?

Simulators may help answer such questions—which apply equally to ground vehicle miles, battalion field training days, and ship steaming days. But the national training centers, if used objectively, are probably the best places for these kinds of tests, especially since interactions with an “enemy” should provide better data than aircraft firing at unresponsive targets.

Long-Term Effectiveness

A more speculative but equally important exercise would be to relate next-generation weapons systems and munitions to future effectiveness and cost. It is tempting, for instance, to “stealth” all future combat air-

craft. But the technology is expensive and may prove vulnerable to countermeasures, and there are substitutes for a fully stealthed combat capability. Longer-range air-to-air and air-to-ground missiles, for example, can probably attack enemy aircraft and other targets as effectively as stealthed aircraft, and at lower risk and cost. Decisionmakers need such comparisons to help decide what equipment to buy and what to expect in the way of operating and support costs.

Finally, much of the concern about future readiness appears to stem from a failure to use properly and improve existing budgetary tools. The planning, programming, budget system put into place more than 30 years ago has undergone only modest changes, but has managed to grow much bureaucratic moss. The five support programs—R&D; central supply and maintenance; training, medical, and other general personnel activities; administration; and support of other nations—comprised more than 37 percent of the program budget in fiscal 1994 but remained unrelated to the six force programs. Moreover, despite the substantial reduction in forces since 1989, the support programs have actually risen by 2 percent (in real terms) relative to the force programs. Does that signify greater waste, increased effectiveness, or something else?

Even if they are not improved, the program budget and the future-years defense program (FYDP) should be treated as serious documents with the potential to relate inputs to outputs. To the extent that secretaries of defense have seen the FYDP as a political rather than a planning document, they have tended to push tough decisions about cost, performance, and balanced forces into a future beyond their responsibilities. Considerable danger exists that this will happen again. Congress, however, can insist that the FYDP clearly show the kinds of emerging problems that have concerned Senator McCain, as well as the costs of resolving them.

It may be convenient to all parties for the Pentagon to tell the president and Congress what ought to be done about the U.S. military establishment and how much it will cost. But the proper responsibility of the Defense Department is to advise both branches of government as to what they can buy in the way of capability at various levels of investment. It is not enough to assert that the forces are going hollow when the budgets are the same as they were 20 years ago, but the forces are smaller and the balances of prior-year budget authority are larger. Systematic evidence of the relationship of inputs to outputs needs to be presented, as well as how changes in resources will change the inputs and outputs. As in other areas, it remains the responsibility of the president and Congress to weigh these changes against the other demands made on the large but finite resources of the federal government.

Defense is the first responsibility of government under the Constitution. Beyond a certain point, however, the needs of defense should compete—in terms of costs and relative increments of effectiveness—with health, education, civil order, and all the other factors that create the conditions of security for the American people. ■



REAL

THE TROUBLE

During the Cold War, “scenario-based” military planning was something of a religion in Washington. We created contingency scenarios that demanded access to airfields across all of central Africa for power projection to the Middle East, or that mandated the “strategic” targeting of grass recovery airfields in the Ukraine, should deterrence fail. We inevitably were able to see contingencies premised on the Soviets sweeping across the north German plain or through the Fulda Gap and on to the Channel in two weeks or less.

The scenario-based approach to planning, to thinking and creating in a national security context, was important then, because it impelled us toward the politico-economic decisions that decisionmakers and legislators wanted and needed to make and were seeking an excuse to implement. After all, how could one justify the national security component of the budget if we did not have a Soviet bogeyman that could be counted on to do things to us? Fortunately for the scenario-based planners, the Soviets obliged with Berlin Crises, Hungary, the Prague Spring, the Cuban Missile Crisis, and the invasion of Afghanistan. We drew conclusions and built forces, and it did not turn out badly in the end.

In this context, scenario-based planning became an intellectual trap for some and an intellectual crutch for others. It provided a seemingly “rational” tool for trying to size military forces and sometimes specious argu-

ments for doing things we wanted to do anyway. Scenario-based planning was useful, but it could also lead us down the garden path with sadly predictable results.

When Events Crash In

Let us consider for a moment some of the other things that actually happened—events that crashed in and gave us a peek at a reality we did not factor into our planning. It is reasonable to ask that, whenever there is a real surprise in the world, the existing set of conclusions drawn from planning scenarios and contingencies be re-examined. We may not change anything, but we should at least do some thinking.

The downing of the Korean airliner KAL 007 is an interesting place to start. Were any scenarios dealing with conflict with the Soviet Union adjusted after the tragedy? Were any weapons programs adjusted or altered as a result? To the best of my knowledge the answer to both questions is negative. Does it make a difference that this is so?

KAL 007 was not the first Korean airliner either shot down or forced down over Soviet territory. But KAL 007 was a large, slow, high-flying, and unarmed Boeing 747. The Soviets had trouble detecting this “target.” Then they had trouble finding it. Moreover, just as they were about to lose it, they had trouble shooting it down. If they had that set of problems with a commercial airliner, how would they have dealt with something as so-

ITY CHECK

**JOHN
THOMAS
TYLER, JR.**

WITH SCENARIO-BASED MILITARY PLANNING

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phisticated, fast, and low as a modernized B-52 or F-111? The question is more than rhetorical, because we have spent a lot of the public's treasure on both the B-1 and B-2. This modern pair of bombers was necessary, of course, to get past the increasingly sophisticated and dense Soviet air defense system—which couldn't deal with a 747.

Another event that crashed in on the scenarios was the young German, Mathias Rust, piloting a small airplane to land in the middle of Red Square. To accomplish this feat, he did not have to be preceded by a wave of F-4G Wild Weasel or EF-111 aircraft blanking out Soviet air defenses. Again, it is highly doubtful that any scenarios—or anything else associated with any defense program—were adjusted to reflect any conclusions that might have been drawn from this real event.

Nor were there ever any planning adjustments—or adjustments to the budget—to reflect what we knew of Soviet maintenance and logistics practices, rampant alcoholism in the Soviet armed forces, the logistics nightmare of changing railroad gauges in the middle of the Warsaw Pact logistics train, or the simple fact that maps of places like Western Europe and its borders were classified top secret—available to those who might have to navigate with them only at the last minute (and thus kept out of the hands of anyone who might use them to plot an escape). Any conclusions that could be drawn from such things did not square with our necessary perceptions of an awesome Soviet



**SCENARIOS AND
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DETERMINED FORCE LEVELS.**

threat. We also did not draw too many conclusions from the rather credible job that Freedom Fighters in Afghanistan did against Soviet forces—especially after we provided Stinger anti-aircraft missiles.

There were, of course, no contingency plans or scenarios that were predicated on the fall of the Berlin Wall—the events of December 1989—and the collapse of the Soviet Union and the Warsaw Pact. One Pentagon planner, however, did say informally in January 1990 that the events of the past month meant that the U.S. Army no longer needed a Main Battle Tank—and certainly not the M1A2. This, of course, was only a matter of months before the Iraqi invasion of Kuwait (not in any scenarios), which triggered the tank-heavy Desert Storm. Reality, the effect of events crashing in, is hard to deal with if you are a national security or a military planner. You can always be accused of not having enough contingencies, enough scenarios. But you cannot afford to do any adjusting to reflect what does happen because of the possible effects on vested interests in the national security community and Congress.

The Arab-Israeli 1973 Yom Kippur War was studied to death by the Defense Department, and one has to wonder if any conclusions were drawn and acted on other than those that supported the current thinking of the day or that simply rationalized buying more ammunition because of high Israeli consumption rates. Did anyone thereafter factor in the reality that Arabs can get their act together, hide it from everybody, and then execute a complicated plan with a disconnected end-game? The surprise attack symbolically restored lost Arab pride and made Anwar Sadat's flight to Jerusalem and the Camp David Accords possible in an Arab context. We certainly did not act on any of the conclusions that could have been drawn as a result of the resupply of Israel in late 1973 and early 1974 about the need for rapid sealift—though we did take some steps to improve our airlift capability. If we had had a little more respect for some aspects of Arab planning, might we have avoided at least some of the surprise of the Kuwait invasion or the extent of Iraq's nuclear program?

Ignoring Reality

One can also posit that there are no scenarios or contingencies that evoke either the type of crisis we are facing in Somalia or the one in Bosnia. The former does not comply with traditional roles and missions requirements; the latter is just too messy and too political. It is much easier to ignore reality and rely on theoretical (or is it theo-rhetorical?) scenarios and contingencies with such labels as “Major Regional Contingency—Europe,” or “Major Regional Contingency—East,” or even “Lesser Regional Contingency—Far.” Another complicating factor is that real countries sometimes have a problem with abstract scenarios—because they see them as applying to themselves. South Korea, for example, has been discomfited with its waiting-for-the-cavalry role as part of a “hold” scenario.

Scenarios and contingency planning can be useful, but not to justify already and politically determined force levels. They are also not honestly useful in the budget war unless resources are unrestrained and you

can play with as many scenarios and contingencies as you want. Scenarios are supposed to follow from predictions of “possible” international events—not be predictions. They are inherently useless as predictors. Nonetheless, people, usually those who do not do national security planning, sometimes ridicule planning scenarios as though they were what was *expected*. This criticism is often self-serving—everyone, it seems, has an agenda.

The basic problem with contingency and scenario-based planning is the tendency to become mired in the process of planning. The thinking becomes too static. It is, quite simply, a lot easier to ignore reality than to change a scenario that has been approved in the course of a budget process and has survived the lowest common denominator approach to military thinking often embodied in the Pentagon staffing process. This did not matter much when the Defense budget was on the rise, when there was a clearly defined Soviet bogeyman as a threat—and when our domestic agenda took second place. Back then scenarios helped provide legislators and pundits a military component to reinforce the politico-economic rationale they needed to support defense spending.

Things are different today. The Soviet bogeyman is gone; he cannot threaten us immediately and credibly any more. When he left he took with him the luxury of the stability and predictability a bipolar world provided. We no longer have a public willing to continue mortgaging the future to support a relatively unconstrained defense budget. Which means that we live in a severely budget-constrained environment.

New Scenarios or New Process?

So the question becomes whether we can find scenarios, reflective of the real world, that can be used to illustrate what we could do with the forces that budget realities will enable us to keep and to build today. If, for example, the budget realities drive us down to less than 100,000 troops in Europe, what conclusions do we draw about how the command structure should look and how adventuresome we can afford to be? Should we change the way we organize to take account of increased reliance on multilateral organizations like the United Nations or NATO? Do budget realities force us into planning scenarios where we actually have to rely on other countries and their forces to achieve success? Does specialization—by other countries—become a necessity within NATO?

The planning and budgeting process is considerably more complicated, both for now and for the longer term. And, in some ways, it is even less amenable than in the past to “rigorous analysis.” Clear thinking, common sense, and a little luck are going to be needed. Intuitively we can identify certain priorities. One example is fast sealift to attenuate the effects of downsizing, fewer overseas bases, and the unpredictability of crises. Even though fast sealift has never been popular with the Navy—it’s not a carrier battle group—it is now being augmented, but only with congressional stimulation. On the other hand, is there a plausible scenario that could not be met with commercial sealift?

A couple of things are likely to happen. We will end

up doing a serious review of roles and missions, uncomfortable as that will be for the military departments. Fiscal realities drive us to the conclusion that we will simply not be able to sustain the programs necessary to support the force structure necessary to support the status quo. Budget pressures will also force us to pay a lot more attention to doing what we can within specified fiscal restraints and less time seeking increases to the budget to support a particular force structure or set of roles and missions.

By engaging in resource-restrained planning—take the pot of money, divide it up, see what force you get, test it against potential threat scenarios, and then adjust for nuance and desired results like readiness—we will probably back into a *real* roles and missions review without a direct confrontation with the military departments. We simply will not be able to “do it all” unless we are willing to grope back in the direction of the hollow force of the 1970s. That could lead to tragic results.

We may actually have to change some behavior as well as some attitudes. This is a key point. Thus, we may have to agree that other nations have some of the same problems, and that while one of us cannot afford everything, maybe we can have it all, together. This prospect does raise the specter of specialization within NATO and even having American troops under the command of a non-American general. That will not be easy. Equally, we will find it harder always to claim the “four-star job.” If or when we sink below 100,000 troops in Europe (especially absent a current Russian, Central or East European threat), our claim to the senior military job in NATO will be tenuous. (But we might build a claim to the right to have the senior political job in NATO.)

The challenge for the planners and thinkers will be to look over the horizon, unfettered by the rhetoric of the past or its perceived truisms. We will live in a resource-driven environment that we have not experienced before. We will need to plan our forces with the resources available and test them carefully against sets of threats and scenarios—and then adjust. And then we will need to test the results again and again as the environment changes. We will have to ask serious questions about how we deal with nontraditional missions such as “peacemaking and peacekeeping” or “promoting proper civil-military relations.” Will we be safer if we have our active forces deployed around the world “keeping peace” (for example, in Cambodia, Bosnia, Somalia, Rwanda, Angola, Liberia, the Sinai, the Golan) than if we have them “in reserve” waiting for—or perhaps deterring—a major regional crisis?

Besides contemplating how we plan, structure, and budget for our forces, we must begin doing some creative thinking (maybe even analysis) about what makes “conventional deterrence” work in the new security context, where the greatest *real* threats to peace may be “tribal” warfare with AK-47s—compounded by hunger, human rights abuses, and the absence of a “sense of security.” This is particularly important as we seem poised to shift from a threat-based force (but-tressed by scenarios) to a capabilities-based force (driven by budget realities). ■

Paychecks or Welfare Checks

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All welfare reform proposals now being considered by Congress aim to move recipients of Aid to Families with Dependent Children off the welfare rolls and into the workforce. Most proponents of reform hope to accomplish this goal within clearly defined time limits. Under President Clinton's plan, young parents would have to accept a public or private job within two years of entering the rolls or see their monthly checks stopped.

In view of tight limits on federal spending, it would be prohibitively expensive to offer publicly funded jobs to all able-bodied AFDC recipients. The work-oriented reform strategy can therefore succeed only if most AFDC recipients find private-sector work. But are there enough private-sector jobs to go around? Will AFDC parents—mostly mothers—be able to find and hold these jobs? And if they do, will former recipients be able to earn enough to support their families on the wages they earn?

The job prospects of AFDC mothers are not very encouraging. Although the educational attainment of poor women is slowly improving, roughly half of single mothers on welfare have not finished high school. Only one in ten has received any schooling beyond high school. Only one in a hundred has graduated from college. Most young women on welfare score in the bottom quarter on standardized tests of general aptitude and ability. Even if welfare recipients had no young children to care for—and almost half have children under six—most would face severe problems finding and holding good jobs.

Earnings Trends among AFDC Recipients

Limited schooling and poor academic achievement doom most AFDC mothers to low-wage, dead-end jobs. Figure 1 compares the 12-year earnings histories of a recent group of young AFDC recipients and another group of women of the same age who did not receive AFDC benefits. The lower line traces the wage gains of young women who collected AFDC during part or all of at least one year between 1979 and 1981. Most of these women left the AFDC rolls after 1981.

Less than a third were still collecting benefits in 1990. The higher line shows average wage gains of a representative group of women who collected no welfare benefits between 1979 and 1981. (A few of these women collected AFDC sometime after 1981, however.) Women in both groups were between 18 and 22 years old in 1979; they were 29 to 33 years old by 1990.

Between 1979 and 1990 the average real wage of the AFDC recipients rose from \$6.18 to \$6.85 an hour—a yearly gain of 6 cents an hour, or less than 1 percent. Among women who did not collect benefits the average wage climbed from \$6.07 to \$10.00 an hour—a yearly gain of 37 cents an hour, or almost 5 percent. (All wage and income figures are measured in constant 1991 dollars.) To put these wage statistics in perspective, consider

their implications for living standards of a single-earner household. Most people in full-time jobs work about 2,000 hours a year—40 hours a week for 50 weeks. Young AFDC recipients and nonrecipients alike could earn a bit more than \$12,000 a year in 1979. By 1990, the AFDC recipients' potential annual earnings had inched up to \$13,700. Nonrecipients' earnings had climbed to \$20,400.

The average wage trend of welfare recipients, slow as it is, exaggerates what many recipients can expect to earn. The wage statistics shown in figure 1 reflect the average wages of women who were *actually at work* during a particular year. In 1987, for example, about half the women who received AFDC between 1979–81 held a job and had a recorded wage. The other half did not work, and the average wage shown for 1987 does not reflect the potential wages of the women who did not work. Since these jobless women, on average, had fewer qualifications than the former AFDC recipients who held jobs, it seems unlikely that they could earn as much as their employed counterparts.

Poverty's Chokehold

Figure 2 shows the implications of the hourly wage trends for year-round earnings levels. The top line traces the predicted annual earnings path of AFDC recipients, assuming that recipients earn the hourly wage shown in the lower line of figure 1 *and* that they work year-round in a full-time job. The line represents a typical AFDC recipient's "potential" full-time earnings path. The middle line traces the average earnings trend among AFDC recipients who *actually worked*, either part-time or full-time during part or all of a given year. In 1979 these working women held jobs for only about 500 hours a year, so they earned just over \$3,000—about a quarter of what they would have earned in a full-time, year-round job. By 1990 their actual earnings were \$10,200, about 75 percent of "potential" full-time earnings.

The bottom line in figure 2 shows the trend in annual earnings among *all* young women who received AFDC between 1979 and 1981, including the women who did not work at all. After 1983 the line begins to climb, both because more women start to work and because annual hours at work among women who hold jobs begins to grow. Even so, by 1990 the average amount of time in a job is less than 1,000 hours a year. AFDC recipients and former AFDC recipients earn less than half what they could have earned in full-time, year-round jobs.

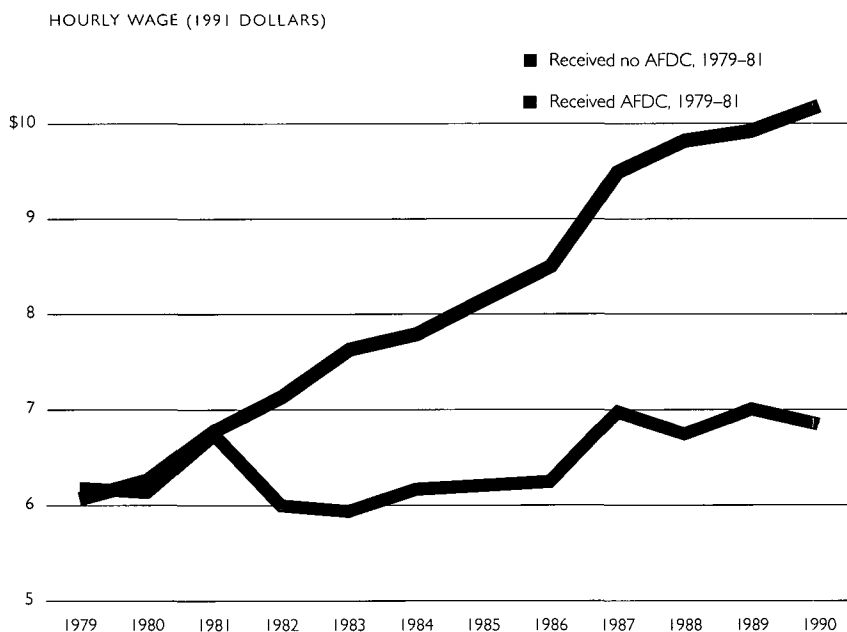
The trends illustrated in figure 2 offer two key lessons for welfare reform. First, single mothers on welfare *can* substantially increase their earnings. Among all young women who received AFDC benefits between 1979 and 1981, real earnings nearly tripled between 1980 and 1990, growing from \$2,300 to \$6,700. Among the working women, earnings more than doubled, rising from \$4,000 to \$10,200.

The second lesson is more disheartening. If all the young women who collected AFDC in 1979–81 had worked full-time in 1990, their average earnings would have been \$13,700. But that was *still* \$200 below the 1991 poverty threshold for a family with one

Gary Burtless

Gary Burtless is a senior fellow in the Brookings Economic Studies program. This article is adapted from a longer paper presented at the Urban Institute conference "Self-Sufficiency and the Low-Wage Labor Market" in April. That paper will appear in Demetra Nightingale and Robert Haveman, eds., The Work Alternative: Welfare Reform and the Realities of the Job Market (Urban Institute, forthcoming).

Figure 1. Average Hourly Wage of Young Women, 1979–1990



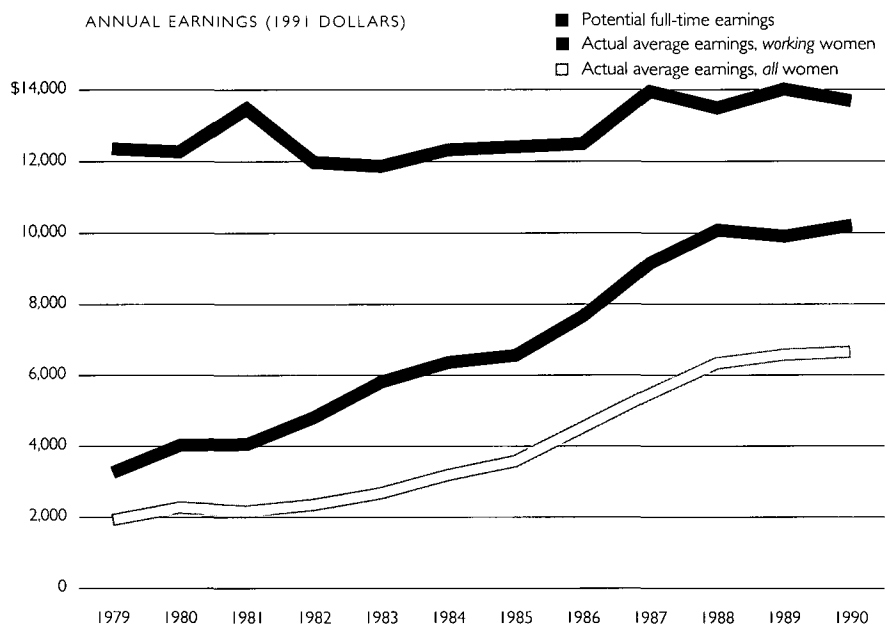
adult and three children. And, as noted earlier, many AFDC recipients cannot realistically expect to earn even that amount.

Another point deserves mention. The welfare caseload includes many women who are on the rolls briefly, others who will receive benefits intermittently, and still others who collect benefits steadily for years. Most welfare reform proposals are aimed at increasing the earnings or changing the behavior of recipients in the last two categories, women who are the most severely disadvantaged. The “potential” full-time earnings shown in figure 2, which reflects the experiences of all three kinds of recipients, substantially overstates the potential earnings of intermittent and long-term recipients. If we could observe the earnings experiences of only the intermittent and long-term recipients, the earnings trends would look considerably worse than those shown in figure 2.

The labor market offers bleak employment prospects to poorly educated single mothers. AFDC recipients cannot easily find jobs that pay high enough wages to support comfortably an adult and one or two children. Even full-time, year-round work would not lift some AFDC recipients and their families out of poverty. Among the young women we have been following, 25 percent of those who managed to find jobs by 1990 earned \$4.69 an hour or less; 10 percent earned \$3.97 or less. A woman earning \$3.97 an hour would have to work 2,500 hours a year—50 hours a week—to earn even \$10,000 a year. And she would still have to find time to care for her children.

The problem for most long-term welfare recipients is not finding jobs. It is finding jobs that permit them to earn enough to keep their families out of poverty.

Figure 2. Actual and Potential Annual Earnings of Women Who Received AFDC in 1979–81



Are There Enough Jobs to Go Around?

An *individual* welfare recipient, if she is able-bodied and moderately resourceful, can almost surely find an employer willing to offer her a job with a low wage and poor fringe benefits. In many urban labor markets, for example, many unskilled jobless workers find work at temporary employment agencies. Although the work is uncertain and often irregular, diligent and persistent workers can usually get temporary jobs, at least occasionally. They can often obtain permanent jobs if they do well on short-term work assignments. Low-wage retailing, business protection and cleaning services, and informal child care offer other unskilled job opportunities.

None of this work is particularly appealing. Little of it offers high wages, good fringe benefits, comfortable working conditions, or solid prospects for future promotion. But such work exists—as millions of unskilled immigrants can attest. Many immigrants arrive in this country suffering from even worse disadvantages than those faced by long-term welfare recipients. Adult immigrants who illegally reside in the United States are rarely eligible to collect government transfers, except emergency medical aid, so they must rely on their own earnings or on help from their relatives to survive. Most rely on their own earnings.

Even though *individual* welfare recipients can find work in the current job market, is it realistic to think

Source: Both figures derived from author's tabulation of the National Longitudinal Survey of Youth (1979–91).

millions could do so on short notice? Many people forced from the welfare rolls would certainly face serious problems. During the second half of the 1980s the U.S. labor force grew by about 2.1 million potential workers a year. Many new entrants were well educated and reasonably highly skilled. Fewer than a quarter were as unskilled as welfare recipients. If the labor force were flooded by an additional 2 million unskilled entrants within a one- or two-year period, employers would need to double or triple their net rate of hiring new unskilled workers. That seems unlikely. Many new jobseekers would probably face long spells of involuntary unemployment. And some who found work would displace other single mothers, pushing up applications for AFDC as jobless mothers were forced to replace lost earnings with public assistance checks.

Still, over the long haul, the U.S. labor market can probably absorb most of the extra workers without a significant rise in joblessness. From 1964 through 1989 the labor force grew by 50.4 million people, while the number of Americans holding jobs climbed by 47.7 million. About 95 percent of new job seekers found jobs, even though the number of people available for work swelled by two-thirds. The unemployment rate rose only slightly, from 5.0 percent to 5.2 percent. To be sure, unemployment climbed steeply in the 1970s and early 1980s, when the labor market was unable to absorb an enormous influx of new entrants. But most of the rise in joblessness in the mid-1970s and early 1980s was due to business cycle movements, not the surge in the work force.

One reason the labor market can absorb so many extra job seekers is that, over the long term, employers can change their production methods to exploit the large supply of low-wage workers. In addition, wages can change in response to the entry or exit of large numbers of labor force participants. In the 1970s, for example, the wages of younger workers fell in relation to those earned by older workers, in part because younger workers became so much more plentiful. Faced with a huge increase in the availability of young workers with limited job experience, employers changed their production methods. Restaurant meals were prepared and served by 11th-graders and high school dropouts rather than by experienced cooks or waiters. Gardening and domestic cleaning chores were performed by unskilled and semiskilled employees rather than by homeowners themselves. In the end, 95 percent of new job seekers found jobs. Unfortunately, few of the new jobs paid princely wages.

If 2 million AFDC recipients were forced to accept private-sector jobs, most would eventually find them. But the inflow of unskilled workers would depress the wages received by other less skilled workers. The wage trends shown in figures 1 and 2 may therefore represent an overly optimistic assessment of the wage prospects of 1 or 2 million welfare recipients if they were suddenly forced to leave the public assistance rolls.

Policy Responses

The potential wages of long-term welfare recipients are extremely low. That does not mean that a work-

oriented welfare strategy is doomed to fail. It does mean that sticks intended to force potential breadwinners off the rolls must be combined with carrots that improve the living standards of recipients who find private-sector jobs.

Although some current welfare reform proposals do not include any new carrots, most do. The president's proposal, for example, includes tough new requirements that would force some noncustodial parents to contribute to the financial support of their children. His proposal also includes additional day care assistance for working single parents. It is unrealistic, however, to expect that small improvements in child support collections or day care assistance will provide much help to long-term recipients who are forced into a hostile labor market.

The administration hopes that other changes in the policy environment will cushion the income loss suffered by single parents who are pushed into private-sector jobs. In 1993 the president proposed, and Congress adopted, a substantial liberalization of the Earned Income Tax Credit, or EITC. This refundable income tax credit, available to low-wage adults who have child dependents, is payable only to people who have earnings. By 1996 the credit will provide as much as \$3,370 in extra after-tax income for a family whose breadwinner works full-time at modest wages. For a single mother who earns low wages, the credit can make the difference between below-poverty earnings and an after-tax income that is modestly above the poverty line.

The administration also tried to extend guaranteed health insurance protection beyond the population that receives public assistance to the entire population of working-age adults and their families. That would relieve some low-wage workers of the need to pay high insurance premiums or heavy bills for uninsured medical expenses. Since unsubsidized medical insurance can easily cost working-age families over \$4,500 a year, this reform would immediately raise the attractiveness of employment for many welfare recipients.

Some proponents of welfare reform are so sure that the stick of time-limited welfare can succeed that they see no need for carrots. Their reasoning is simple: if young people knew that welfare benefits would be tightly restricted, fewer of them would engage in behavior that leads to public dependency and more of them would take steps to improve their chances of finding or keeping a good job. In the short run, public dependency would fall; in the long run, child poverty could shrink.

This theory, though plausible, remains unproven. The evidence on actual wages earned by single mothers is less subject to dispute. The data in figures 1 and 2 suggest that in the short run a large minority of current welfare recipients—and their children—would face extreme hardship if forced to rely solely on earnings for their support. Confronted with this harsh reality, many voters will find it hard to accept strict time limits on welfare unless they are accompanied by a perceptible improvement in the earnings prospects of mothers who will be pushed off the rolls. ■

Promises, Promises

WILLIAM
R. LOWRY

As another summer fades, so does political attention to the plight of America's national parks. Last spring, as the thoughts of millions of Americans turned to the cool mountain air and fresh, clear streams of their parks, the Clinton administration's spokesman, Interior Secretary Bruce Babbitt, promised to "lay out our vision of where we want to take the national parks in the next three years." That promise, and others like it, reflected another effort by the administration to avoid neglect of the "vision thing" that plagued the Bush presidency. But what has been missing in American parks policy—and what has remained in short supply during the Clinton presidency—is not vision, but the political courage to see preservation become a reality.

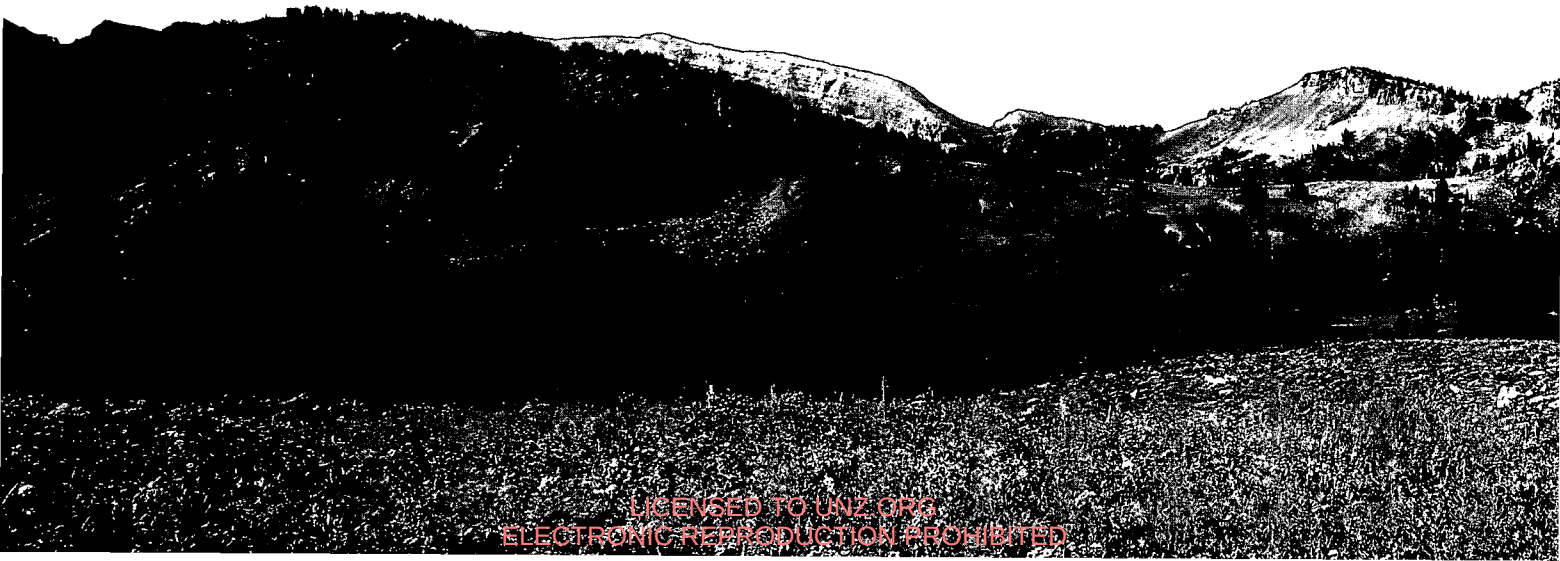
The vision of parks as wilderness preserved under natural conditions has been explicit in American political thought since 1872. In legislation setting aside Yellowstone that year, Congress called for "the preservation, from injury or spoliation, of all timber, mineral deposits, natural curiosities, or wonders . . . and their retention in their natural condition." In the years since, Americans have entrusted to the National Park Service more than 360 parks or other units, a small (less than 4 percent of the nation's total) but precious land area, to be preserved "unimpaired for the enjoyment of future generations."

But many of America's national parks—and indeed the Park Service itself—are now in trouble.

Smog, Crime, Politics

One obvious problem is lack of money. Throughout the 1980s and early 1990s, the Park Service's budget hovered around \$1 billion a year, even though total visits to the parks increased more than 25 percent. As a result of increased use and simple aging, the parks now have a backlog of nearly \$2.2 billion in infrastructure repairs. Park visitors, for example, find that more than one-third of all roads in the parks need repairs. Crime is also on the rise. More than 40,000 crimes, including 6,500 major ones, were committed in the parks last year. Because staffing has not grown commensurately, more and more Park Service employees must be detailed to crime prevention, and fewer are available for interpretive and preservation programs. External threats to the parks—air pollution, water pollution, commercial encroachment—have also increased dramatically. Visitors now find *in* the parks much of the congestion, smog, and urban blight they had hoped to leave behind. Air pollution from recently built power plants in Virginia, for example, has reduced annual average visibility on Shenandoah's Skyline Drive from a natural figure of 80 miles to today's 15.

With park entrance fees rising of late, one might have expected increased park use to provide a revenue windfall for the Park Service. Indeed, many visitors accept the higher entrance fees and inflated prices for concessions such as food and lodging, believing that they are contributing to Park Service revenue. But congressional authorization of higher entrance fees in 1986 diverted entrance fee revenue to the General Treasury Fund, where it can be used for



WILL AMERICA'S NATIONAL PARKS BE PRESERVED?

everything from welfare to defense. And the average return to the federal government from concessions is only 2.5 percent.

The Park Service budget has also been stretched by haphazard expansion of the system. Often expansion is driven by politics. The classic example is Steamtown National Historic Site in Scranton, Pennsylvania. Steamtown came under the Park Service in 1986 when Scranton's congressman, Joe McDade, bypassed the formal procedures for park creation, using his clout as ranking minority member of the House Appropriations Committee to amend a pending omnibus bill. Over the next six years, nearly \$70 million was appropriated to convert an abandoned rail yard with no original equipment into what a panel of historians testified to Congress was "little more than a railroad theme park with an eclectic collection of trains." Meanwhile, plans to preserve natural conditions in other parks, such as the one formulated in 1980 to relieve automobile congestion in Yosemite Valley, remained unrealized for lack of money. Nor is Steamtown alone. In 1990, several Park Service personnel complained in a memo that the agency was becoming a "repository for what are in essence economic development type projects." Indeed, a bitter standing joke inside the agency is that it would more appropriately be named the "National Pork Service."

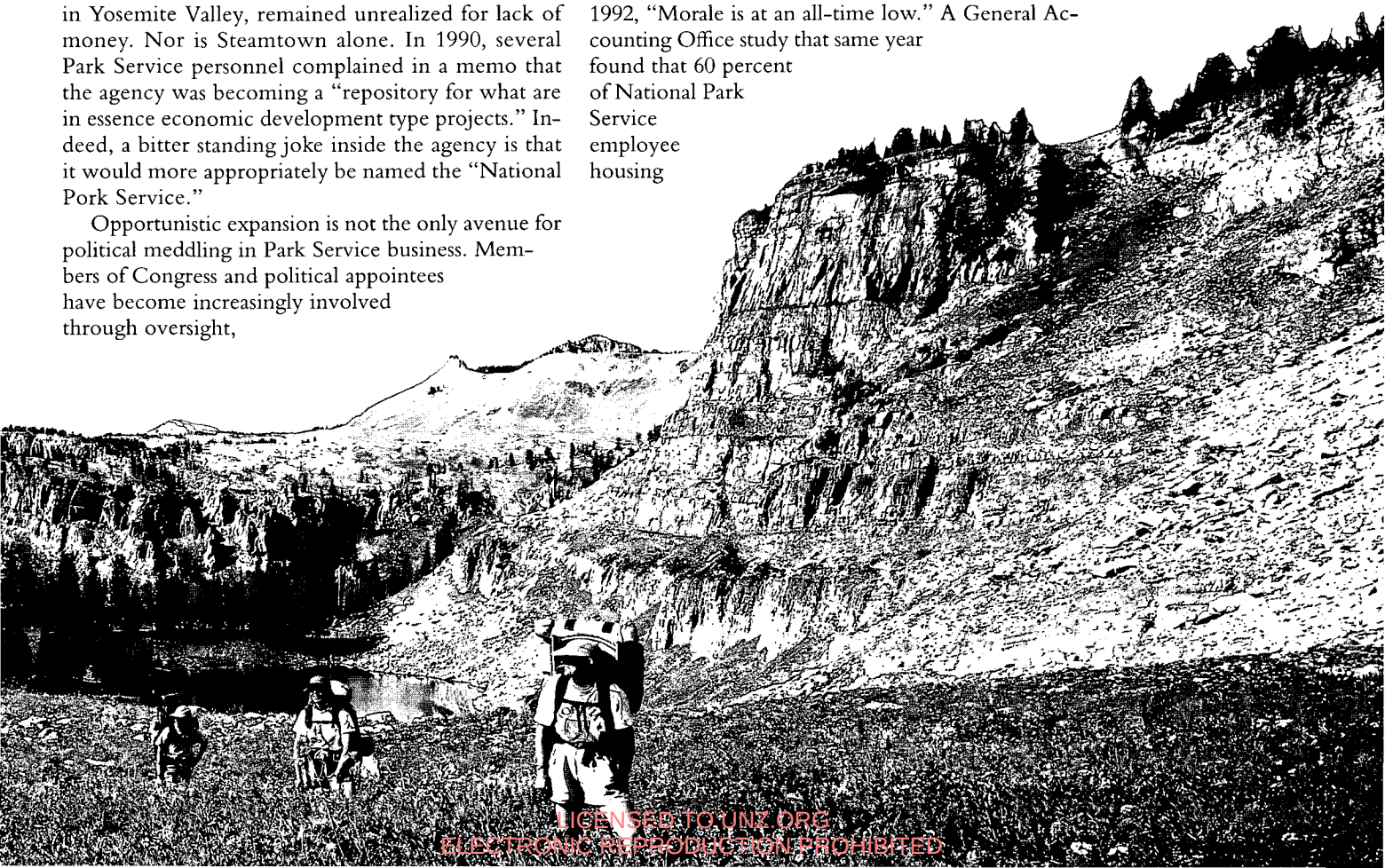
Opportunistic expansion is not the only avenue for political meddling in Park Service business. Members of Congress and political appointees have become increasingly involved through oversight,

constituent casework, financial control, manipulation of personnel, and policy decisions. Too often, as Yosemite superintendent Mike Finley told me, "Decisions are made for politics instead of for the resource." Two examples suffice. In 1974 park officials trying to improve bear management in Yellowstone proposed to remove one commercial settlement, Fishing Bridge, in prime grizzly bear habitat and, in exchange, to build a new one, also in prime bear habitat, at Grant Village. Today, commercial operations continue at both at the insistence of the Wyoming congressional delegation—what one superintendent called "policy consideration beyond Yellowstone." In 1979 the Park Service called for the complete phase-out of motorized craft from the Colorado River in the Grand Canyon. But the plan was scuttled by Senator Orrin Hatch (R-UT). The agency's own internal 1992 assessment terms the Park Service "overrun" by political intervention.

According to one Park Service field manager in 1992, "Morale is at an all-time low." A General Accounting Office study that same year found that 60 percent of National Park Service employee housing

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PHOTOGRAPH BY NEIL GILCHRIST.
PANORAMIC IMAGES



needed repairs—at an estimated cost of \$500 million. Pay scales have stagnated while the cost of living has gone up, resulting in much higher than normal employee turnover. In their 1992 self-appraisal, Park Service employees concluded, “There is a wide and discouraging gap between the service’s potential and its current state, and the service has arrived at a crossroads in its history.”

Tough Enough?

Discouraged Park Service personnel—and park supporters generally—took heart from Clinton administration promises of a renewed emphasis on preservation in park policy. Vice President Gore, Interior Secretary Babbitt, and Assistant Secretary George Frampton, Jr., were all prominent environmental advocates. On appointing Babbitt, Clinton insisted, “The Secretary of the Interior must be tough enough to stand up to powerful interests.” National Parks and Conservation Association president Paul Pritchard said of Babbitt, “We can count on him to care for and be committed to our national parks.” Historian Robin Winks wrote in a *New York Times* editorial, “For the first time in 12 years the American people have a chance to reclaim their national parks.” Editors of the *Economist* speculated that “the wilderness may flourish again.”

Administration rhetoric has sustained that enthusiasm. Babbitt promised a “substantial increase” in the Park Service budget to go along with more emphasis on preservation and expansion. On a visit to Yosemite, he urged a return to the goals of the Park Service’s 1980 plan for reducing traffic and emphasizing mass transit. Last May the administration unveiled National Park Week with numerous festivities promising greater attention to park problems.

Nothing New

But the administration’s *record* has fallen short. As in so many other issues facing the Clinton presidency, vision has often exceeded political courage. A willingness to compromise—an eagerness to please all sides—may be easy politically, but it does not undo the damage of the past.

Talk is cheap. Protecting parks is not. The promised “substantial” increase for the Park Service budget in 1993 was anything but. The \$984 million operating budget in 1993 was slightly higher than that in 1992, but adjusted for inflation, it purchased fewer services. The 1994 operating budget saw a 9 percent increase, but that was offset by cuts in other areas such as acquisitions. The total budget grew only 3.9 percent. The proposed 1995 budget would increase operations (6 percent), but cut construction (26 percent) and acquisitions (22 percent). The small increases going to the parks are not nearly enough.

In decisions on individual parks, again, administration performance has not matched expectations. Babbitt made several promising early decisions such as reversing construction of the Cape Hatteras National Seashore jetties approved by President Bush in the days before the 1992 election. In many parks, however, the biggest changes seen in 1993 were cutbacks

in services through such means as trimming interpretive programs, reducing visitor center hours, and closing campgrounds. And even those cutbacks continue to be politically determined. For example, Shenandoah officials who proposed closing part of the Skyline Drive in winter months to save \$200,000 were overruled by Virginia’s congressional delegation, who were concerned about “severe economic consequences” for constituents in neighboring Front Royal. In a highly publicized case, in July of last year, the administration released a new plan for the Everglades that it claimed would stop the devastating diversion of fresh water out of the park and reduce pollution washing in from nearby farms. In fact, the plan compromised on the timetable for pollution reduction and on the imposed costs to sugar growers. Even so, disputes over the compromise plan returned the case to court last April.

The morale of the Park Service has improved, but only slightly. Agency employees are thankful that problems affecting the parks are at least getting official attention. But they are still skeptical that political commitment will follow. During National Park Week, a Park Service employee grumbled, “Because this is parks week we have to put on a show, but there’s nothing new to say.”

Why is there nothing new to say? The anecdote about Shenandoah suggests one reason. Many of the changes expected from the Clinton administration are beyond their control. Many policy decisions affecting parks are determined in Congress. And political manipulation of Park Service actions is not confined to Republicans. In addition, budget changes are historically incremental. Most of the shortages in Park Service financing, accumulated over decades, will not be easily remedied. Finally, changing some of the specific arrangements affecting the parks will take time. Concession contracts, for example, are issued for up to 30 years.

This is not to let the administration off the hook. Clinton and his appointees have not fully used the tools available to them in attempting to change Park Service practice. Budget proposals have been less than bold. Political appointees in public lands policy have hardly been reform zealots. In itself, the selection of the Smithsonian’s Roger Kennedy over the National Parks and Conservation Association’s Paul Pritchard to head the Park Service signaled a backpedaling from the administration’s initial rhetoric. The most outspoken appointee in public lands policy, Bureau of Land Management Director Jim Baca, was forced to resign by Babbitt earlier this year after complaints from western ranching and farming interests, the same interests that made the administration back down on land use fee reforms. Presidents can also propose structural reorganizations, but the Park Service remains part of the Interior Department despite calls by Pritchard and other park supporters to make it an independent agency. Indeed, the closest the administration has come to proposing a reorganization of the Park Service has been to discuss “downsizing” the agency. Finally, the president enjoys access to the fabled “bully pulpit,” but Clinton has remained largely silent on national parks issues.

A bitter standing joke inside the National Park Service is that it would more appropriately be named the “National Pork Service.”

What Can Be Done?

To live up to its promises to restore the original vision of the parks, the administration can take several steps. The first is simply to reaffirm the original mandate for the Park Service, making preservation the dominant and explicit goal of the agency. Representative Bruce Vento's (D-MN) proposed National Parks and Landmarks Conservation Act will provide a good starting point. The proposal calls for a five-year term for the director of the Park Service, a commitment to a systematic research program, and explicit recognition that units of the Park Service “be accorded the highest degree of protection feasible.”

Second, the administration should provide the Park Service more resources. Admittedly that is a difficult proposition given the fiscal situation, but several possibilities exist. First, the existing system for awarding concessions contracts is an acknowledged mess. Contracts are awarded on a near-monopoly basis with long durations (15 to 30 years), low rates of return (a 1990 average of 2.5 percent on gross sales), and often preferential right of renewal. Senator Dale Bumpers (D-AR) has introduced legislation that would reform the system by emphasizing competitive bidding, shorter contracts, and higher returns to the government. Second, user fees are a good candidate for park revenues. The Interior Department has again proposed to raise entrance and user fees. The proposal warrants support as long as it is written to guarantee higher returns to the Park Service.

Boondoggles like Steamtown can be avoided by using a systematic procedure for expanding the park system. The House Natural Resources Committee has proposed a long-range expansion plan using scientific analysis of potential new units. Congressional meddling with the Park Service's limited resources might also be reduced by closing the loophole in the 1935 Historic Sites Act that allows appropriations for projects not authorized through the normal committee channels.

Finally the administration would do well to consider reorganizing the environmental policy bureaucracy. As it stands, the Park Service is housed in a cabinet department with agencies whose missions are often contrary to preservation ideals. The Interior Department is now responsible not only for preserv-

ing parks (Park Service) and preserving endangered species (the Fish and Wildlife Service), but also for strip mining (Office of Strip Mining Reclamation and Enforcement), grazing (Bureau of Land Management), and Native American issues (Bureau of Indian Affairs). National forests, commonly located adjacent to parklands, are managed by the Forest Service in the Agriculture Department. Coordination of effective responses to various problems is now quite difficult. For example, imagine a river flowing through rangelands and forests before entering parklands. The Park Service has no control over pollution and use of the river outside park grounds. Rather than making the Park Service an independent agency, as some have proposed, the administration could create a new Department of the Environment, modeled on the Canadian system. (Attempts to establish such a department were made in both the Nixon and Carter administrations.) The department could bring together not only the Fish and Wildlife Service and the Park Service, but also the Forest Service. Coordinated actions by these agencies would help address difficult situations, including external threats such as encroachment and pollution.

In essence, the administration needs to find ways to give the Park Service the authority and discretion to do the job. The Canadians have recently done just that by decentralizing powers within the Canadian Parks Service. We could start with implementing the Park Service plans already existing in places like Yosemite, Grand Canyon, and Yellowstone.

As the Clinton administration has learned so many times, change is never easy. Successful change requires vision and courage. With national parks, a vision has been built through a century of foresight and the desires of millions of park visitors who simply want a portion of this country to be kept as relatively natural wilderness. Seeing that vision become reality will take the courage to confront commercial operations with a vested interest in the status quo, the courage to counteract political authorities who have used the parks to satisfy the demands of specific constituencies, and the courage to seek additional funding for national parks in tough economic times. Promises won't do it. ■



Global Change

INCREASING ECONOMIC INTEGRATION AND ERODING POLITICAL SOVEREIGNTY

**RALPH C.
BRYANT**

Two fundamental facts characterize the political and economic structure of the world at the end of the 20th century. First, the world is, and for the foreseeable future will be, organized politically into nation-states with sovereign governments. Second, increasing economic integration among nations has been eroding the differences among national economies and undermining the autonomy of national governments, a trend that also shows no sign of stopping.

International economic interdependence has significantly improved standards of living for most nations and promises further sizable benefits. Yet the heightened competition between national political sovereignty and increased cross-border economic integration could cause major trouble if national policies and international cooperation are poorly managed.

Increasing World Economic Integration

Profound technological, social, and cultural changes have bound the world's nations more closely together by reducing the effective economic distances among them. The same transportation and communication wizardry that makes it easier and cheaper for companies in Ohio to ship goods to California, for residents of Marseilles to visit relatives in Paris, and for investors in Hokkaido to buy and sell shares on the Tokyo Stock Exchange also speeds trade, migration, and capital movements among nations and continents. Technology has, in effect, shrunk the planet.

Consumers and producers are increasingly aware of potentially profitable international exchanges and of economic opportunities abroad. Foreign goods, foreign vacations, and foreign financial investments were once exotic but are now virtually commonplace.

Communications technology has especially boosted financial activity. Computers, switching devices, and

The opportunities and tensions arising from the competition between cross-border economic integration and national political sovereignty are the focus of a major Brookings project, entitled Integrating National Economies. Scholars from a variety of disciplines have produced 22 studies for the project, to be published over the course of the next year. In this article Ralph C. Bryant identifies some important themes and issues common to all these studies. For a complete list of the studies, contact the Brookings Marketing Department or call toll-free 1-800-275-1447.

telecommunications satellites have slashed the cost of transmitting information internationally, of confirming transactions, and of paying for transactions. Forty years ago foreign exchange could be bought and sold only during business hours in the initiating party's time zone. Now large banks pass the management of their worldwide foreign-exchange positions around the globe from one branch to another, staying continuously ahead of the setting sun.

Government policies have reinforced the effects of technology. Before World War II nations routinely erected "separation fences" at their borders—taxing goods moving in international trade, directly restricting imports and exports, and curbing financial exchanges between domestic and foreign residents. The effect was to reduce cross-border transactions, sometimes even to eliminate them. The particularly zealous use of these policies during the 1930s is now believed to have deepened and lengthened the Great Depression.

After the war, most national governments began, sometimes unilaterally, more often collaboratively, to lower these fences, to poke holes in them, or sometimes even to jettison parts of them altogether. The international negotiations under the auspices of the General Agreement on Trade and Tariffs (GATT)—for example, the Kennedy Round in the 1960s, the Tokyo Round in the 1970s, and most recently the protracted negotiations of the Uruguay Round, formally signed only last April—stand out as the most prominent examples of fence lowering for trade in goods. Though contentious and only partially successful, the GATT negotiations sharply reduced at-the-border restrictions on trade in goods and services.

The fences barring financial transactions were lowered later and to less dramatic effect. Nonetheless, by the 1990s curbs on capital flows, especially among the industrial countries, were much less important and widespread than they had been during the 1950s.

The recent strides in technology alone would have substantially integrated the world economy—as would the lower trade fences alone. But together, the two have reinforced each other and profoundly transformed the world economy.

Changes in the Government of Nations

As the world's nations have grown together economically, the world's political structure has also changed markedly. Since World War II the number of nation-states has grown rapidly, and political power has been diffused more broadly among them. Rising nationalism and, in some areas, heightened ethnic tensions have accompanied that increasing political pluralism.

Only 44 nations participated in the July 1944 Bretton Woods conference that gave birth to the International Monetary Fund. By the end of 1970, the IMF had 118 member nations; by the mid-1980s, 150; by December 1993, 178. Much of this growth reflects the collapse of colonial empires. While many nations today are small and carry little individual

weight in the global economy, their combined influence is considerable and their interests can no longer be as easily ignored.

Over the years the United States gradually lost its political and economic hegemony. Immediately after World War II, the United States alone accounted for more than a third of world production. By the early 1990s, the U.S. share had fallen to about one fifth. The political and economic influence of the European colonial powers also waned while the economic significance of nations such as Japan, Korea, Indonesia, China, Brazil, and Mexico grew. A world once dominated by one or a few nations has yielded to one in which economic power and influence are widely shared.

Turmoil and prospects for fundamental changes in the formerly centrally planned economies have been still other forces radically transforming world politics. Governments that for years tried to isolate their economies are now trying to adopt reforms modeled on Western capitalist principles. To the extent they succeed, those nations' economies will increasingly become integrated with the global economy. Political and economic alignments among Western industrialized nations will be forced to adapt.

Dilemmas for National Policies

Unfortunately for the peace of mind of nations' policymakers, the interplay between the trends of enhanced economic integration and increasing political pluralism tends to generate discord. Each trend has exacerbated a mismatch between the economic and political structures of the world. The effective domains of economic markets have come to coincide less and less well with national governmental jurisdictions.

When the separation fences at nations' borders were high, governments and citizens could easily distinguish "international" from "domestic" policies. International policies dealt with at-the-border barriers (for example, tariffs) or events abroad. Domestic policies involved everything behind the nation's borders—for example, competition and antitrust rules, corporate governance, product standards, worker safety, regulation and supervision of financial institutions, environmental protection, tax codes, and the government's budget. Domestic policies were treated as a sovereign preserve, to be determined by the preferences of the nation's citizens and its political institutions, without regard for effects on other nations.

With economic integration, however, the differences in nations' domestic policies, formerly neglected, have increasingly been exposed to international scrutiny. Accordingly, national governments and international negotiations have been confronted with numerous issues of deeper, behind-the-border integration. For example, if country A permits manufacturers to emit air and water pollutants whereas country B does not, companies that use pollution-generating methods of production will find it cheaper to produce in country A. Manufacturers in country B that compete worldwide with those in country A are likely to complain and to press for international pollution standards.

Many issues of this type have already complicated negotiations over the evolution of the European Com-

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munity, the GATT Uruguay Round, and the North American Free Trade Agreement. As time goes on, debates about behind-the-border policies will occur more and more often and prove at least as complex and contentious as past negotiations over at-the-border barriers.

Cross-Border Spillovers and Diminished National Autonomy

A chief source of tensions is activities in one nation whose economic consequences spill across borders and affect other nations. Such spillovers in turn make it more difficult for governments to control events within their borders.

Illustrations abound. Lax banking and securities regulations in one nation undermine the ability of all to enforce their regulations and deal with fraudulent transactions. When one nation pollutes the air or water that other nations breathe or drink, it becomes a matter for international negotiation. Spillovers between national financial markets erode the power of any one nation's central bank to maintain monetary conditions different from those in other countries.

The tensions resulting from cross-border spillovers and diminished autonomy can be particularly vexing when national policies are alleged to be competitively unfair, as in a dispute where manufacturers in country A emit pollutants and those in country B do not. Likewise, if country C requires all goods, whether produced at home or abroad, to meet safety or labor standards that foreign competitors find too expensive to meet, C's standards effectively limit or even eliminate foreign competition for its own producers. Citing examples of this sort, producers or governments in individual nations often complain that business is not conducted on a "level playing field." Typically, the complaining nation proposes that *other* nations adjust their policies to moderate or remove the competitive inequities.

Yet international trade exists precisely because of differences among nations—in resource endowments, labor skills, and consumer tastes. Nations produce goods and services in which they are relatively most efficient. In a fundamental sense, cross-border trade is valuable because the playing field is *not* level. When David Ricardo first developed the theory of comparative advantage early in the 19th century, he focused on national differences in technology or climate. Today the "climatic" differences are often social, not physical. But the theory of comparative advantage, taking all differences into account, continues to argue validly that free trade among nations will typically maximize global welfare.

It is unrealistic, even pernicious, to suppose that all nations can be made homogeneous in every important respect. Suppose country A decides that it is too poor to afford a clean environment and that it will permit production of goods that pollute local air and water supplies—or that it cannot afford stringent safety standards. It will then argue that other nations should not impute to it the high value they place on a clean environment and stringent safety standards (just as A should not impose its valuations on other nations). The essence of political sovereignty is that national residents be able to order their lives and property in accord with their own preferences.

Which perspective is more compelling? Is country A merely exercising its national preferences and appropriately exploiting its comparative advantage in goods that are dirty or dangerous to produce? Or does a legitimate problem exist that justifies pressure from other nations urging country A to change its policies (thus curbing its national sovereignty)?

Challenges to Political Sovereignty

In today's world political system, a nation's residents are presumed free to select their own political arrangements without interference from outsiders. Property rights, too, are allocated by nation. (The "global commons," such as outer space and the deep seabed, are the sole exception.) A nation is assumed to have the sovereign right to choose how to use its own property.

Although some nations have had sovereignty wrested from them by force in times of war, until recently few people have questioned the premises of political sovereignty. Today, however, more and more people and groups—occasionally even national governments—are claiming that, under certain circumstances, a more universal or international set of values should override the preferences or policies of particular nations.

Environmental groups from many nations, for example, characterize tropical rain forests as the lungs of the world and as the genetic repository for numerous species of plants and animals. Regarding those forests as the heritage of all mankind, Americans, Europeans, and Japanese challenge the timber-cutting policies of Brazilians and Indonesians. Likewise, many citizens worldwide found South Africa's apartheid policies an affront to universal values and denied that the government legitimately represented the majority of the nation's people. Many national governments thus banded together to apply economic sanctions against South Africa.

A common feature of cases of this type is the presence, real or alleged, of what can be termed "psychological externalities" or "political failures." Those who challenge conventional national politics from these perspectives insist on the international community's right to constrain the exercise of individual nations' sovereignties through negotiations or, if necessary, even stronger intervention.

Options for Managing International Convergence

For issues where cross-border spillovers are weak and psychological externalities or political failures may be minor (for example, education and road-building expenditures), national governments encounter few problems stemming from the increasing integration of the global economy. Diversity across nations may persist relatively easily. But at the other extreme, for issues where spillovers are strong and political sensitivities are asserted powerfully, diversity in nations' policies will be contentious and may even be impossible. For such issues national policies and behaviors may eventually have to converge to common, worldwide patterns. Whether such convergence proves harmful (national policies and practices being driven to a least common denominator, in effect a "race to the bottom") or mutually beneficial ("survival of the fittest and the best") will depend on how governments manage the transition.

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Economic convergence could be managed in a variety of ways. At one extreme of a continuum—the traditional practice for most of this century—national governments could persist in making decisions unilaterally, relying solely on market competition to guide convergence. A more cooperative approach, known as mutual recognition, assumes that governments make separate decisions, but exchange information and consult with each other to constrain formation of national regulations and policies. Each member state of the European Union, for example, agrees to accept, in many policy areas, the regulations, standards, and certification procedures of other EU members. Wine or liquor produced in any EU country can be sold in all 12 member countries despite differing production standards. Doctors licensed in France are permitted to practice in Germany, and vice versa, even if licensing procedures in the two countries differ.

Going further in the direction of cooperation, governments could mutually monitor each other's behavior (as happens in the Group of Seven finance ministers meetings) and agree on guidelines or rules that restrict their freedom to set independent policies. More ambitiously, governments could "coordinate" by jointly designing and mutually adjusting policies, as for example in the World Health Organization's procedures for controlling communicable diseases and the 1987 Montreal Protocol for protecting stratospheric ozone by reducing emissions of chlorofluorocarbons.

Harmonized "regional standards" or "world standards," as in the 1988 agreement among major central banks to set minimum ratios for the required capital positions of commercial banks, require still higher levels of intergovernmental cooperation. Finally, at the other extreme of the continuum, governments could engage in continuous bargaining and joint, centralized decision-making. This last approach to managing economic convergence, however, is of only theoretical interest for now, and can be imagined only for the middle or late decades of the 21st century.

Political Challenges for the Future

Clearly, economic integration poses many challenges for national governments. All the issues have complex economic dimensions, and governments must better understand the economic costs and benefits involved before they can choose sound national policies and the most appropriate management options for cooperating with other governments.

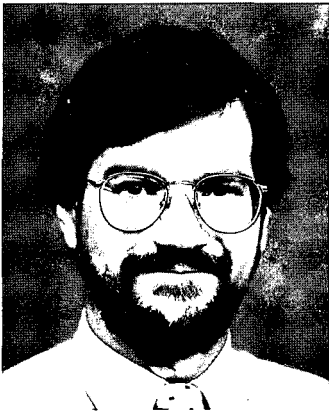
Nonetheless, the most profound challenges are political. Existing political institutions within nations and the nascent international institutions cannot plausibly stand still: "business as usual" will not be viable.

To be sure, the useful concept of "subsidiarity"—the presumption that decentralized allocations and exercises of political power are to be preferred absent compelling reasons for centralization—provides a solid foundation for retaining many governmental decisions at the national (and even local) level. For many functional issues, the option of mutual recognition of separately decided national policies is an appealing first-recourse approach to managing international convergence. In effect, national governments would choose decentralized decisions and mutual recognition where possible, would coordinate decisions when necessary, and would centralize decisions or delegate authority to an international institution only when mutual recognition and coordination were shown to be unworkable.

Even with a heavy emphasis on subsidiarity, however, national governments must develop and nurture many varieties of cooperation. Still more important, domestic political institutions must evolve in ways that are responsive to the world's pervasive drift toward behind-the-border integration. The rapid pace at which economic behavior has become internationalized has far outstripped the adaptation of political institutions. This gap—in effect, a burgeoning political deficit—will have to be narrowed if the world economy and polity are to evolve satisfactorily in the 21st century. ■

Peace in Civil War: A Dilemma

BY STEPHEN JOHN STEDMAN



Though one is a world emblem of genocide and the other of reconciliation, both Rwanda and South Africa highlight a moral and practical dilemma for the international community in dealing with civil war: the pursuit of accountability of those responsible for war crimes and the dictates of negotiation.

This past May the Rwandan Patriotic Front dismissed calls to resume peace negotiations with the government to end the Rwandan civil war. Liking the government's slaughter of a half million Tutsis and moderate Hutus to the Nazi elimination of Jews, the RPF compared its situation with that of allied forces in May 1945 who were within kilometers of Berlin and complete victory over Hitler. Why, it asked, would anyone now demand that it negotiate peace? Where was support from the international community for its demand to try the government for war crimes?

In South Africa, talks are under way on the merits of establishing a commission to investigate war crimes and civilian massacres over the past eight years. While many South Africans object that such a commission would interfere with reconciliation—a feeling seconded by Western governments—others wonder why war crimes should be investigated in Bosnia, but not in South Africa.

In the rest of Southern Africa, where negotiation has ended civil wars in Zimbabwe, Namibia, and Mozambique, the balance of power between adversaries and the necessities of negotiation have dictated a policy of “don’t ask, don’t tell, and don’t pursue” toward persons involved in atrocities.

By contrast, in Bosnia mediators have been hampered by Western demands that a settle-

ment not sacrifice accountability, that war crimes be investigated and tried. Until recently, the United States disdained mediation for fear of bloodying its hands with a peace that rewarded Serbian aggression.

Such repugnance toward the moral exigencies of peacemaking in civil war is new for the United States. It pushed for a peace settlement in Cambodia that did not mention Khmer Rouge crimes against humanity. It applauded the maturity and pragmatism of new governments in Southern Africa for repudiating the investigation of war crimes. And, as suggested by Rwanda, America’s urge to resolve civil war morally is not universally applied.

If the international community is to forge a consistent policy toward the peacemaking-war crimes dilemma, the key must be the practical judgment of whether a particular civil war is negotiable.

Until recently, civil wars were thought to be nonnegotiable. But since 1979, numerous civil wars—including those in Zimbabwe, Namibia, South Africa, El Salvador, and Nicaragua—have been ended through negotiation.

Policymakers now assume that all civil wars are negotiable. Thus the U.S. and French insistence, as late as the middle of June and amidst continuing massacres by Rwandan government forces, that the warring sides in Rwanda negotiate. But those hopes for negotiation begged a crucial question: what would the Rwandan government have had to do to convince reasonable observers that it was not interested in making peace?

The crisis in Rwanda mirrored one of Southern Africa’s failed settlements. In Angola, like Rwanda, a negotiated settlement promised to end

a long, bloody conflict. In both cases, spoilers reneged on their commitment to peace when it became clear to them that they would not win through settlement what eluded them on the battlefield. Both UNITA in Angola and the Presidential Guard in Rwanda used the cease-fire to strengthen themselves in preparation for reverting to war. In Rwanda, like Angola, violence in the months after the peace agreement collapsed was worse than in the years of war before the agreement. And, in both, the world response to the crisis was to urge the victims to renegotiate the terms of the peace through appeasing the spoilers.

The carnage of civil wars, their protracted nature, and the spillover effects on neighbors all dictate that the world community try to resolve them. The moral concern for saving lives must take priority over the moral concern of justice for the victims. Where negotiation can succeed, accountability for war crimes will have to be abandoned.

But some civil wars cannot end through negotiation. Some parties in civil war define the struggle as all-or-nothing and will use negotiation and settlement as a tactic to defeat their adversaries. Such parties can only be defeated; they cannot be appeased through negotiation.

Parties such as those in Rwanda and Angola who violate peace agreements and plunge their countries back into yet bloodier war should be held accountable and tried for crimes against humanity. To urge negotiations, as the United States and France did in Rwanda and as the United States did in Angola, fails to draw moral distinctions among combatants, exonerates parties accountable for genocide, and ignores that some civil wars are not negotiable. ■

Stephen John Stedman is an assistant professor of African studies and comparative politics at the Johns Hopkins University School of Advanced International Studies. He is coauthor, with Thomas Ohlson and Robert Davies, of The New Is Not Yet Born: Conflict Resolution in Southern Africa (Brookings, 1994).

GATT: Where Are the Trumpets?

BY SUSAN M. COLLINS AND BARRY P. BOSWORTH

The recently completed Uruguay Round of the General Agreement on Tariffs and Trade is a landmark achievement that deserves far more general recognition and discussion than it has received. Unlike the seven earlier GATT agreements, which focused rather narrowly on liberalizing trade in goods, this one looks ahead to the increasingly complex international economic relations of the 21st century.

The first six GATT negotiating sessions significantly reduced world tariffs—from an average of 40 percent among industrial countries in 1948 to an average of just 6.4 percent today. The seventh session, the Tokyo Round (1973–79), began to expand the agenda, addressing some concerns about proliferating quantitative restrictions, such as trade quotas, and other nontariff barriers. The Uruguay Round has moved further down this road, for example finally reaching agreement to phase out the Multi-Fibre Agreement that restricts trade in apparel.

Some observers are disappointed with the Uruguay Round because it achieved less traditional trade liberalization than they had hoped. For instance, negotiators were unable to make much headway in reducing trade barriers in agriculture, agreeing instead on new rules and means of measuring protection that may lead to more liberalization in the future. Still, estimates are that trade liberalization engineered in the Uruguay Round may eventually raise world income by roughly 1 percent of GNP from improved allocation of resources—with perhaps an additional 1 percent increase from increased investment and other “dynamic” gains. Critics have characterized these benefits as small, but it is hard to think of other actions by governments with equivalent returns.

As international economic relations grow more complex, it is no longer enough for GATT to focus only on liberalizing trade in goods. Services, for example, now account for a fifth of global trade, and this share is growing. Further, expanding international linkages make it harder to separate at-the-border trade barriers from the behind-the-border regulations and practices that countries can use to discriminate against foreign goods. Thus, harmonious cross-national economic relations will require a structure capable of reconciling disputes arising from a broad range of cross-national differences.

Although GATT’s founders never envisaged it in such an over-arching role, negotiators in the Uruguay Round made a serious attempt to enable the GATT to address a much broader agenda. Notably, they negotiated new agreements to cover trade in some service sectors and to discipline the use of intellectual property—both areas of particular interest to the United States because they are so closely related to its areas of comparative advantage. Perhaps most significant, they created a new institution, the World Trade Organization, to help implement the rules of these agreements. Under the WTO structure, member nations would be required to accede to all major GATT provisions—certainly a step ahead of the current structure (often called “GATT a la carte”) that enables countries to pick and choose among them. Further, the WTO develops a more sophisticated mechanism for settling trade disputes, significantly reducing the problem of countries blocking reports on their own discriminatory trade practices at various stages of the procedure.

Whether the agreement will live up to its promise is another

matter. The agreement on services makes more progress in establishing rules and procedures than in liberalizing trade per se. The new dispute mechanism may do little to improve compliance, especially by larger countries. But in many respects, the new GATT agreement is simply a beginning. Much will need to be worked out along the way.

Why has the agreement received so little attention? One reason is the prominence of so many other important public issues, including health care, the crime bill, and developments in Haiti. A second is that, unlike the noisy 1993 debate over the North American Free Trade Agreement, the domestic opposition has not been particularly vocal, so supporters have seen little need to trumpet the agreement’s benefits.

A third reason for the lack of attention is that the “winners” of the Uruguay Round are a group that is diffuse, and in some cases, hard to identify. This tends to be true of all agreements to liberalize trade, because the major beneficiaries are consumers—typically spread across regional, income, and other groupings—who gain from access to more varied or lower-priced products. But it is even more true of the Uruguay Round agreement, because many of the achievements are procedural. For example, even though many observers expect the United States to benefit from the revised dispute settlement mechanisms, the actual U.S. winners will emerge only over the coming years.

The central point is that the upside potential from the Uruguay Round agreement is great. While only time will tell whether it in fact grows up to fulfill its promise, surely such a beginning deserves a few trumpets. ■



Susan M. Collins and Barry P. Bosworth are senior fellows in the Brookings Economic Studies program. Susan Collins is also associate professor of economics at Georgetown University. The two are co-editors of The New GATT: Implications for the United States (Brookings, 1994).

Americans Who Don't Give a Damn

BY STEPHEN HESS



This November, in what many expect to be the most significant midterm congressional election since the Water-gate year, 1974, two out of three eligible Americans will not vote.

This stunning fact of non-participation in the simplest, easiest, and most basic act of civic duty can no longer be explained as it was to me 40 years ago.

Political science courses then told us that nonvoting was a product of two factors. The first was roadblocks erected for racist or political reasons, the poll tax and literacy tests in the South, exclusionary registration requirements in the North. The second was demographics, specifically the presence of a large unschooled class, voting being highly correlated with education.

Now, of course, there are no poll taxes, no literacy tests, and few restrictions to inhibit turnout. Moreover, when the Cox Newspapers surveyed 2,809 Americans in 1988, they found that of those who don't vote, 20 percent had less than a high school education, 43 percent were high school graduates, 20 percent had some college, and 17 percent were college graduates. (Indeed, several years ago I discovered that my college roommate doesn't vote!)

Where should we place our public responsibilities in the scheme of things? John Adams once wrote to his wife Abigail, "I must study politics and war that my sons may have liberty to study mathematics and philosophy. My sons ought to study mathematics and philosophy . . . in order to give their children a right to study painting, poetry, music, architecture." Our

second president had his priorities right. Americans are quite wonderfully—up to a point—an apolitical people. Yet voting is the occasional act of citizenship that if exercised wisely permits us to study painting and poetry.

There can be a rational reason for not voting, namely when the choice makes no difference. This is a time of exceptional partisanship in Congress, however. Two-thirds of the roll call votes in the House and Senate split along party lines in 1993. It simply isn't possible to conclude that there are no differences between Democrats and Republicans.

Americans now appear to have massively turned off on current events that aren't salacious or don't involve a celebrity. In March the Times Mirror Center for the People and the Press released the results of this five-question quiz:

- What country is threatening to withdraw from the nuclear nonproliferation treaty?
- Which ethnic group has conquered much of Bosnia?
- Which group recently reached a peace accord with Israel?
- Who is the president of Russia?
- Who is the secretary-general of the United Nations?

Thirty-seven percent got all five questions wrong. (Six percent got all five right.) Other recent polls show Americans' knowledge about what Congress is doing to be equally deficient. In one instance, for example, a quarter of the respondents thought Congress had passed a mythical bill to control immigration.

A July headline in the *Washington Post* read "Six out

of Ten Disapprove of Way Hill Does Its Job." Given the state of the public's ignorance, this is not criticism, it is whining. Some blame the educational system, others the media. Nonsense. Both have faults galore. Still, schools teach reading; newspapers, radio, and TV disseminate basic information. The fault is not that Americans can't read or listen.

At the same time, politicians prefer to pander. As do talk radio hosts. In the 1960s a senator from Ohio named Stephen Young wrote a constituent, "Dear Sir: I thought you should know that some idiot sent me a letter and signed your name." Where are the Steve Youngs today?

Millions of Americans take seriously their civic responsibilities, contribute their time and energy to their communities, and, of course, vote. What is also clear, and will be proved again on November 8, is that the vast majority of Americans don't give a damn. ■

Stephen Hess is a senior fellow in the Brookings Governmental Studies program. The author of Live from Capitol Hill! Studies of Congress and the Media (Brookings, 1991), he is completing International Coverage in the U.S. News Media.

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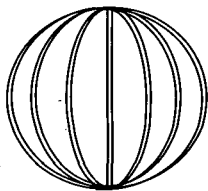
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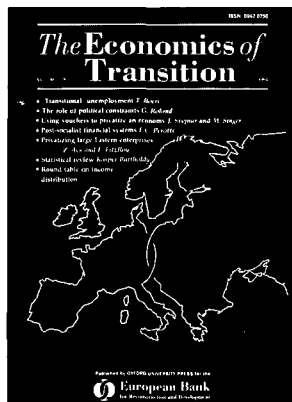
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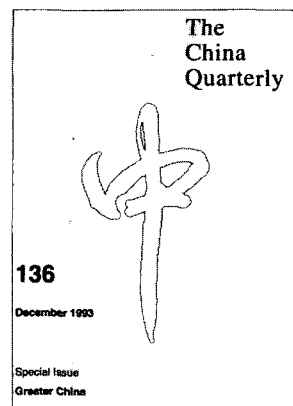
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